No. 936

IN THE

SUPREME COURT OF THE UNITED STATES.

OCTOBER TERM, 1946.

ST. LOUIS SOUTHWESTERN RAILWAY COMPANY,
a Corporation, Debtor,
Petitioner,

vs.

BERRYMAN HENWOOD, as Trustee of ST. LOUIS SOUTHWESTERN RAILWAY COMPANY LINES, et al.,
Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE EIGHTH CIRCUIT

and

BRIEF IN SUPPORT THEREOF.

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To the United States Circuit Court of Appeals for the Eighth Circuit.

To the Honorable the Chief Justice of the United States, and to the Associate Justices of the Supreme Court of the United States:

Your Petitioner, St. Louis Southwestern Railway Company, a Corporation, Debtor, the appellant in the above captioned case in the United States Circuit Court of Appeals for the Eighth Circuit, numbered 12882 therein, prays that a writ of certiorari issue to review the opinion and judgment of that court. Said judgment (R. 5559-5683) affirmed, substantially, the order of the United States District Court for the Eastern District of Missouri (R. 5183-5213) approving the plan of reorganization for Debtor certified by the Interstate Commerce Commission under Section 77 of the Bankruptcy Act (11 U. S. C. Sec. 205) (R. 3495-3733, 3736-3820).

SUMMARY STATEMENT OF THE MATTER INVOLVED.

The St. Louis Southwestern Railway Company, a Missouri Corporation, Debtor, on December 12, 1935, filed in the District Court of the United States for the Eastern Division of the Eastern Judicial District of Missouri, a voluntary petition for reorganization under Section 77 of the Bankruptcy Act (11 U. S. C. Sec. 205) (R. 24). On the same day a copy of the petition was filed with the Interstate Commerce Commission (R. 26). The District Court entered an order approving the Debtor's petition on December 12, 1935 (R. 27, 256).

The Debtor filed its proposed plan of reorganization with the Interstate Commerce Commission on December 7, 1936, and other plans were subsequently submitted (R. 258). Hearings on the proposed plans were held before the Commission during March and April of 1937 (R. 96 et seq.). Additional hearings were held before the Commission from May 5, 1939 to May 27, 1939, and from September 18, 1939 to September 30, 1939 (R. 529-3049).

On June 30, 1941, the Commission submitted its Report and Order approving a plan of reorganization for the Debtor (R. 3495-3733). Various petitions for modification of the plan were filed with the Commission (R. 3736-3737). Under date of March 9, 1942, a supplemental Report and Order were issued by the Commission disposing of the petitions theretofore filed and modifying in some minor respects its original report of June 30, 1941. As thus modified, the Commission again approved the plan of reorganization for the Debtor which had been approved by the report of June 30, 1941 (R. 3736-3820).

The existing capitalization of the Road was found to be the sum of $105,944,706, including loans and bills pay-

able as of January 1, 1942 (R. 3785). The Commission approved a capitalization of $75,000,000, of which 50 per cent is funded debt, 25 per cent preferred stock, and 25 per cent common stock (R. 3692, 3774). In reaching this result, the Commission adhered to its original conclusion which was stated by it as follows (R. 3700):

> "Thus, debt claims totaling $8,304,118 can receive no recognition within the limits of capitalization approved. From a consideration of the entire record, including the elements of value referred to, the earnings and prospective earnings, and especially the impairment in earning power of the properties, we conclude and find that this result cannot be avoided. Consistently therewith, we further find that the equities of the holders of the stock of the debtor have no value."

In due time various parties in interest filed objections to the report, and to the plan as approved by the Commission under date of March 9, 1942, effective January 1, 1942 (R. 3828, 3835, 3840, 3849, 3854, 4011).

A hearing was had before Judge Davis between the dates of October 26, 1942 and November 5, 1942 upon Debtor's objections and the exceptions of the other parties to the Report and Order of the Interstate Commerce Commission and its supplemental report. Evidence was taken at considerable length (R. 4051-5136) and a date set for arguments. Prior to the arguments and before the briefs of the various objectors had been filed, Judge Davis died. Thereafter Judge Moore made an order directing a reargument on May 31, 1943, and taking the cause as submitted on the record made before the late Judge Davis (R. 5137-5183).

On February 8, 1944, the District Court made and entered an order approving the plan of reorganization certified to it by the Commission (R. 5183-5213).

Appeals were taken to the United States Circuit Court of Appeals by Debtor, by Southern Pacific Company, Intervener, by Horace A. Davis and others as a protective committee for holders of Central Arkansas and Eastern Railroad Company First Mortgage Bonds, Interveners, by Horace A. Davis and others as a protective committee for holders of Stephenville North & South Texas Railway Company First Mortgage Bonds, Interveners, and by Walter E. Meyer, Intervener.[1] These appeals were consolidated and heard upon a single record by the Court of Appeals.

On August 26, 1946, the Circuit Court of Appeals handed down its opinion (R. 5559-5680) affirming the order of the District Court in approving the plan, except for matters not pertinent to this petition, and remanding the case to the District Court for the purpose of amending the plan (R. 5681-5683).

After an order extending the time therefor (R. 5683-5684), petitions for rehearing were filed by the various appellants (R. 5685, 5711, 5767), and on October 22, 1946 were denied (R. 5831).

On November 8, 1946 the Circuit Court of Appeals entered its order staying the mandate for a period of 60 days (R. 5834). Thereafter, upon motion, the mandate was further stayed until January 22, 1947.

The provisions made for the various creditors and stockholders of the Debtor by the modified plan of the Interstate Commerce Commission are set out effectively in the table (R. 3785) therein designated Appendix A. It appears therefrom that the following obligations of the Debtor were left undisturbed: Equipment obligations in the amount of $216,000; First Mortgage Certificates in the amount of $20,000,000; Gray's Point Terminal obligations

1 These appeals were numbered 12882, 12883, 12884, 12885, and 12886, respectively.

in the amount of $500,000; Shreveport Bridge obligations in the amount of $450,000 and Texarkana Union Station certificates in the amount of $315,000. The Railroad Credit Corporation received full recognition of its claim by the allocation of $1,331,300 in ten-year four per cent serial notes. Consolidated Mortgage fifty-year four per cent obligations were issued for the full amount due on the second mortgage certificates and for portions of the claims represented by the First Terminal and Unifying Five's, and General and Refunding Five's and for portions of the claims of Chase National Bank, Mississippi Valley Trust Company and Southern Pacific Company. Five per cent preferred stock was issued for the balance of the claim of the First Terminal and Unifying Five's, and for portions of the balances of the claims of General and Refunding Five's, Chase National Bank, Mississippi Valley Trust Company and Southern Pacific Company. Common stock was issued for the balance of the claim of the General and Refunding Five's, Chase National Bank, Mississippi Valley Trust Company and Southern Pacific Company. Common stock was also issued for portions of the claims of the Stephenville Five's and the Central Arkansas and Eastern Five's. The preferred stock and the common stock of the Debtor were completely eliminated by this plan. The revised plan of the Interstate Commerce Commission, therefore, provided for funded debt in the amount of $37,499,827; five per cent preferred stock in the amount of $18,750,091 and common stock in the amount of $18,749,961, or a total capitalization of $74,999,879.

Before the United States District Court and again before the United States Circuit Court of Appeals the Debtor has consistently contended that the plan proposed by the Interstate Commerce Commission is inequitable for the reason that during the period of time which has elapsed between the filing of the petition herein on December 12, 1935, and

the decision by the District Judge on February 9, 1944, the position of the Debtor had changed from one of insolvency to solvency by a distinct margin. Debtor contended in its appeal that the plan therefore was unjust and inequitable to the stockholders of the Debtor, both common and preferred, in eliminating them completely from the reorganization; that the plan of reorganization should be resubmitted to the Commission for revision in the light of the supervening solvency of the Debtor; that the plan of the Commission gave no consideration to the recent prosperity of the Debtor, the recent accretions to its assets in the form of cash and improvements of the Debtor's financial condition, and the growth in wealth and population of the trade area served by the Debtor; and that the action of the Commission deprived the common and preferred stockholders of the Debtor of their property without due process of law in contravention of the Fifth Amendment to the Constitution of the United States.

The Circuit Court of Appeals discussed these contentions of the Debtor. With regard to the prospective earnings the Circuit Court of Appeals said (R. 5657-5658):

> "The sole cause of these enormous increases is, for the most part if not entirely, the war. This cause was temporary. That the end of hostilities would result in a pronounced decrease to peacetime normalcy is a certainty. * * *"
>
> "It is urged that though there will be a falling off in revenue at the end of the war, yet there will be an increase of business for Debtor over that before war. The argument is that the increase of population into this territory during the war will result in many of these newcomers remaining; and that many of the numerous war industries established there will be converted into peacetime uses. These results may occur but the measure of them is not even estimated. Such uncertain elements can find no place in estimated future earning for reorganization valuation purposes. * * *"

"Whatever may be the effects of these wartime revenues in other relations, they are too abnormal and too temporary to be taken as any gauge of prospective earning of Debtor during the long sweep of years intended by Congress to be planned for in a reorganization proceeding."

With regard to the rise in value the Circuit Court of Appeals had this to say (R. 5662):

"The fact that the physical properties, including cash and liquid securities, may have a value beyond the total indebtedness is not controlling either at the beginning or during such reorganization proceedings. The only place for bettered conditions, after formation of a Plan by the Commission, is where such conditions have so altered the situation as to make the Plan inequitable to existing creditors or stockholders. * * *"

(R. 5663):

"Solvency in the sense of balance of assets over liabilities has small bearing upon such equity.

"The broad question is, do these changed conditions show such inequity in this Plan?"

Later the court makes this comment (R. 5669):

"That these much improved conditions as to cash, liquid assets and potential tax refunds **might** alter the picture as seen by the Commission at the time of its report seems true. However, that they **must** do so because otherwise the sight of the Commission would have to be declared arbitrary, we think is not true."

Petitioner contends that the actual facts now existing in this reorganization are such as to make the Circuit Court of Appeals' doubts about Debtor's future wholly unjustified.

Petitioner submits that the plan recommended by the Commission has become stale and that if equity is to be

done the plan must be re-examined in the light of the drastically changed conditions. We are now in the twelfth year since the date of the filing of the petition by the Debtor. The latest figures which the Interstate Commerce Commission had upon which to base its modified plan were the figures as of December 31, 1941, which figures are now over five years old. These figures reflected none of the tremendous profits made by Debtor during the war period, for the war had commenced only twenty-two days prior to the latest effective date of these figures. Since that time an insolvent corporation has become a solvent corporation by a large margin, giving clear and definite values to the stockholders of the Debtor; yet the plan herein proposed would completely and forever wipe out these definite, real and existing values.

Debtor attaches as Appendix A hereto a table showing the long-term debt, the interest in default and the net current assets of the Debtor as of six dates. The first of these dates is December 31, 1941, the last complete year prior to the promulgation of the modified plan by the Interstate Commerce Commission on March 9, 1942. The next date is December 31, 1943, being the last complete year prior to the United States District Court's approval on February 9, 1944, of the Interstate Commerce Commission's plan of reorganization. The next date is December 31, 1944, being the last complete year prior to the submission of the plan on April 7, 1945, to the United States Circuit Court of Appeals. The next date, December 31, 1945, is included for completeness. The next figures are those of July 31, 1946, which are the latest figures the Court of Appeals could have considered in denying the Debtor's petition for rehearing. The last figures, those of October 31, 1946, are included as the latest available figures. This procedure was accepted by this court in **Ecker v. Western Pacific R. Corp.**, 318 U. S. 448, 507, 87 L. Ed. 892, 949.

An analysis of these figures reveals some startling comparisons. It shows improvement in the Debtor's financial position from the various dates to the present time so pronounced as to take this case out of any of the situations which existed in the cases heretofore decided by this court involving railroad reorganizations, in all of which this court had held that the change in circumstances did not warrant resubmission of the plan, to-wit: **Ecker v. Western Pacific R. Corp.**, 318 U. S. 448, 87 L. Ed. 892; **Group of Institutional Investors v. Chicago, Milwaukee, St. Paul & Pacific R. Co.**, 318 U. S. 523, 87 L. Ed. 959; **R. F. C. v. Denver & Rio Grande Western R. R. Co.**, 90 L. Ed. 1134.

For purposes of convenience petitioner sets forth herein a summary of these changes.

ST. LOUIS SOUTHWESTERN RAILWAY LINES

Improvement in Financial Position from December 31, 1941 (the Last Complete Year Prior to I. C. C. Promulgation of Final Plan on March 9, 1942) to October 31, 1946.

	December 31, 1941	October 31, 1946	Improvement
Long-term Debt	$68,705,399	$67,254,145	$ 1,451,254
Interest in Default	13,862,823	4,690,826	9,171,997
Net Current Assets	8,010,813	22,090,504	14,079,691
Total Improvement			$24,702,942

ST. LOUIS SOUTHWESTERN RAILWAY LINES

Improvement in Financial Position from December 31, 1943 (the Last Complete Year Prior to U. S. District Court's Approval of the I. C. C. Plan of Reorganization on February 9, 1944) to October 31, 1946.

	December 31, 1943	October 31, 1946	Improvement
Long-term Debt	$68,175,434	$67,254,145	$ 921,289
Interest in Default	11,936,783	4,690,826	7,245,957
Net Current Assets	13,440,090	22,090,504	8,650,414
Total Improvement			$16,817,660

ST. LOUIS SOUTHWESTERN RAILWAY LINES

Improvement in Financial Position from December 31, 1944 (the Last Complete Year Prior to Submission of Plan to U. S. Circuit Court of Appeals on April 7, 1945) to October 31, 1946.

	December 31, 1944	October 31, 1946	Improvement
Long-term Debt	$67,866,134	$67,254,145	$ 611,989
Interest in Default	10,056,493	4,690,826	5,365,667
Net Current Assets	14,177,297	22,090,504	7,913,207
Total Improvement			$13,890,863

ST. LOUIS SOUTHWESTERN RAILWAY LINES

Improvement in Financial Position from July 31, 1946 (the Date for Figures Used in Debtor's Petition for Rehearing in the U. S. Circuit Court of Appeals) to October 31, 1946.

	July 31, 1946	October 31, 1946	Improvement
Long-term Debt	$67,636,394	$67,254,145	$ 382,249
Interest in Default	4,190,921	4,690,826	—499,905
Net Current Assets	20,476,594	22,090,504	1,613,910
Total Improvement			$ 1,496,254

It will thus be seen that from December 31, 1941 (the date of the latest figures available to the Interstate Commerce Commission) to the present time, the financial position of the Debtor has changed for the better by $24,702,942. Bearing in mind that the total capitalization contemplated by the Interstate Commerce Commission plan is approximately $75,000,000, it is apparent that the improvement in Debtor's cash position since the formulation and promulgation of the plan is one-third the amount of the total contemplated capitalization.

From December 31, 1943 (the last full year prior to the District Court's approval) until the present time, the financial position of the Debtor has improved by $16,817,660. From December 31, 1944 (the last complete year prior to submission of the plan to the United States Circuit Court of Appeals) to the present time, the financial position of the Debtor has improved by $13,890,863. From July 31, 1946, the date of the figures used in Debtor's petition for rehear-

ing in the United States Circuit Court of Appeals, to October 31, 1946 (the date of the latest available figures), the improvement in financial position has been $1,496,254.

The improvement in the Debtor's cash asset position in the last mentioned amount for three months indicates that the Debtor's financial position is currently improving at the rate of almost $6,000,000 per year.

Bearing in mind that V-J Day occurred in August of 1945, the figures showing the improvement between July 31, 1946 and October 31, 1946, are highly significant in that they show financial improvement at the rate of approximately $6,000,000 a year more than one full year after the actual termination of the war.

There is submitted with this petition as Appendix B thereto the general balance sheet of the Debtor Company as of October 31, 1946 (eliminating inter-company items).

Supplementing the astonishing revelations made by the figures hereinabove cited with reference to decrease in funded debt and over-due interest unpaid and the increase in net current assets, is the increase in the account of Debtor's property devoted to railway service. Despite substantial abandonments of unprofitable lines, and in the face of the Trusteeship, Debtor's investment in road and equipment has continued to grow as follows:

Road and Equipment Property (Including Improvements on Leased Railway Property) as of Various Dates.

Date	Page of Record	Amount
December 31, 1941	5259	$124,808,960
December 31, 1943	5259	$128,465,630
December 31, 1944	5259	$132,647,575
December 31, 1945	5694	$136,493,793
October 31, 1946	Note	$136,577,314

Note: See Appendix B to this Petition.

From December 31, 1941 (the year end nearest to the Commission's promulgation of the plan of reorganization on March 9, 1942) to December 31, 1943 (the year end nearest the District Court's confirmation of this plan of February 9, 1944) Debtor's investment in road and equipment had risen from $124,808,960 to $128,465,630, an increase of $3,656,670. From December 31, 1941 to December 31, 1944 (the year end nearest to the submission to the Court of Appeals on April 7, 1945) Debtor's road and equipment account had risen from $124,808,960 to $132,647,575, an increase of $7,838,615. From December 31, 1941 to the latest available date, October 31, 1946, Debtor's road and equipment account had risen from $124,808,960 to $136,577,314, or an increase of $11,768,354.

These increases in investment in road and equipment are proper additions to the improvement in the financial position of the Debtor for the dates in question.

Based upon all of the foregoing, the total improvement in property and financial situation of the Debtor from December 31, 1941 to October 31, 1946 has been $36,471,296 as indicated by the table hereinafter set forth:

	December 31, 1941	October 31, 1946	Improvement
Long-term Debt	$ 68,705,399	$ 67,254,145	$ 1,451,254
Interest in Default	13,862,823	4,690,826	9,171,997
Net Current Assets	8,010,813	22,090,504	14,079,691
Road & Equip. Property	124,808,960	136,577,314	11,768,354
Total Improvement in Property and Financial Situation			$36,471,296

It is apparent, therefore, that since the Interstate Commerce Commission evolved a plan fixing the total capitalization of the Debtor Road at approximately $75,000,000, there has been a total improvement in property and financial situation of the Debtor Road of more than $36,000,000; in other words, of almost one-half of the total authorized

capitalization set up by the Interstate Commerce Commission.

Obviously, such a definite and unquestionable financial improvement in the Debtor Road presents a situation for the consideration of this court which has never heretofore been before it.

The Commission appraised the Debtor's road and equipment as of December 31, 1935 at $68,523,903 and found that deferred maintenance amounting to $3,173,500 had accumulated (R. 260-262; 3499-3502). The undisputed testimony of Colonel Green, Chief Operating Officer for the Trustee of the Debtor, offered and received at the hearing before the District Court in October, 1942, completely disposes of the item of deferred maintenance. He testified that he had been connected with the Debtor since the year 1916; that since the appointment of the Trustee he had been with the Trustee continuously in the operation of the railroad and that he had charge of the construction, engineering, transportation, mechanical, maintenance of way and certain minor departments (R. 4147-4148). This witness testified that between January 1, 1936 and January 1, 1942 this item of deferred maintenance ($3,173,500) "has all been wiped out; no longer exists" (R. 4149-4151). It is submitted, therefore, that the reason given by the Commission for this item of depreciation did not exist at the time of the hearing in the District Court.

It may be admitted that Debtor was insolvent, in the bankruptcy sense of the word, at the time the petition was filed in the District Court on December 12, 1935. At the time the Commission approved a plan of reorganization it found that debt claims totalling $8,304,118 could receive no recognition within the limits of capitalization approved (R. 3700). In other words, the Commission found that as

of March 9, 1942, Debtor had liabilities exceeding its assets of $8,304,118. The latest figures the Commission had before it were those of December 31, 1941. At this time (December 31, 1941) the net current asset balance of Debtor was $8,010,813 (R. 5259, 5261), and its long-term debt and accrued interest amounted to $82,568,222 (R. 5259-5261).

As of December 31, 1944, the net current asset balance was $14,177,297 and the total long-term debt and accrued interest in default was $77,922,627. The improvement, therefore, during this period of time was $10,812,079. Therefore, the insolvency of $8,304,118 had been entirely wiped out and debtor was then solvent by approximately $2,500,000. As shown by the figures hereinabove set forth, as of October 31, 1946, the comparable net current asset balance was $22,090,504.54 and the long-term debt and accrued interest in default was $71,944,971.96. This represents an improvement over the figures considered by the Commission of $24,702,942. Debtor, therefore, was solvent as of October 31, 1946 by a margin of approximately $16,400,000.

Petitioner attaches as Appendix C hereto, the income account of Debtor for the first ten months of 1946. This shows a net income for these ten months of $3,446,085.12. A projection of this net income would indicate an annual net income for the year 1946 of $4,135,302.14. Appendix C shows the income available for fixed charges for the first ten months of 1946 to be $5,949,631.47. Projecting this figure on a yearly basis, it would appear that the income available for fixed charges this year would be approximately $7,139,557.76. Footnote 17 to the Circuit Court of Appeals opinion (R. 5657) shows the income available for fixed charges from the years 1923 through 1944. It is highly significant to note that during the entire period preceding the year 1941 at no time did this figure exceed

the 1923 figure of $5,929,628. Looking at the period from 1930 to 1940 the highest figure for any one year was the figure of $3,333,243 for the year 1936. It will be noted that the estimated income available for fixed charges during 1946 is more than twice this figure. The 1946 figure is approximately six times the low figures appearing during the ten-year period from 1930 to 1940. The significance of this comparison is apparent from the fact that this is the period upon which the Interstate Commerce Commission largely relied in reaching its conclusions (R. 3504).

According to the plan of the Interstate Commerce Commission, the annual charges ahead of common stock consist of $1,513,723 interest and $937,505 in preferred stock dividends, or a total of $2,451,228. The estimated income available for fixed charges for the year 1946 is approximately three times this amount. Certainly this is a comfortable margin of income over and above the requirements of the proposed capitalization of the Debtor Railroad.

Moreover, these figures prove unjustified the pessimism of the Circuit Court of Appeals which predicted a decrease to "peacetime normalcy" (R. 5658).

There is every reason to expect that these net profit figures will continue to be greatly in excess of the requirements of the proposed capitalization. The court can and will take judicial notice of the extensive population increase and industrial development in the geographical area served by the Debtor Railroad.[2]

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2 The population of Los Angeles as of January, 1946 was 1,805,687, an increase of 20 per cent since April 1, 1940 (Census Bureau Report, Series P-SC No. 119, April 10, 1945). Houston, Dallas and Ft. Worth have grown from 1940 census figures of 384,514, 294,734 and 177,662, respectively, to 478,000, 425,000 and 235,000. The total California population increase from April 1, 1940 to July 1, 1945 was 27.7 per cent. The total Texas population increase between April 1, 1940 and July 1, 1945 was 5.8 per cent (Census Bureau Report Series P-46, No. 3). The total population of the United States as a whole during the same period increased only .2 per cent.

Moreover, considerably augmented gross revenues and attendant net revenues will be derived as a result of the order of the Interstate Commerce Commission made December 5, 1946 in Ex Parte No. 162, Increased Railway Rates, Fares and Charges, 1946, and Ex Parte No. 148, Increased Railway Rates, Fares and Charges, 1942. The effect thereof is an increase in basic freight rates of 20 per cent for the future and the continuation of previously granted passenger fare increases.

With present unquestioned solvency of the Debtor and with a new post-war level of revenues established, it is inescapable that the plan based on figures now more than five years old is inequitable and should not be sustained.

JURISDICTION.

The final judgment of the Circuit Court of Appeals was entered August 26, 1946 (R. 5681). On September 9, 1946, the said court issued an order extending to September 25, 1946 the time for filing petitions for rehearing, which time would otherwise have expired September 10, 1946 (R. 5683, 5684). Petitioner filed its petition for rehearing on September 25, 1946 (R. 5710). This petition was denied by the Court of Appeals October 22, 1946 (R. 5831).

Jurisdiction of this court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925 (28 U. S. C. Sec. 347 [a]) and under Section 24 of the Bankruptcy Act, as amended June 22, 1938 (11 U. S. C. Sec. 47).

This court's jurisdiction is supported by the following cases:

Ecker v. Western Pacific R. Corp., 318 U. S. 448, 87 L. Ed. 892;

Group of Investors v. Milwaukee R. Co., 318 U. S. 523, 87 L. Ed. 959;
R. F. C. v. Denver & Rio Grande Western R. R. Co., 90 L. Ed. 1134.

THE QUESTIONS PRESENTED.

The questions presented are:

1. Whether an Interstate Commerce Commission plan can be sustained as equitable which completely excludes the interests of the stockholders of Debtor from participation, where, as of the present time, the Debtor is solvent by a distinct and unquestionable margin?

2. Whether Debtor's present solvency may be ignored and all of the stockholders' real and valuable interests be wiped out merely because the Interstate Commerce Commission found almost five years ago that there were no equities?

3. Whether a plan which destroys the obvious values of stockholders and excludes them from any future interest or participation in the future development of the company is "fair and equitable," or "affords due recognition to the rights of each class of creditors and stockholders," or "does not discriminate unfairly in favor of any class of creditors or stockholders," or "will conform to the requirements of the law of the land regarding the participation of various classes of creditors and stockholders," as required by Section 77 of the Bankruptcy Act?

4. Whether to deprive stockholders of their legal property, viz., proprietary interests in a corporation, now solvent by a wide margin, does not violate Amendment V to the United States Constitution and amount to a deprivation of property without due process of law?

5. Whether an Interstate Commerce Commission plan can be sustained as equitable when the plan was based on the Debtor's pre-war peacetime level although the Debtor's established post-war peacetime level is considerably higher?

6. Whether in determining the prospective earnings of the property of Debtor, present earnings may be disregarded and the equities of the stockholders be held without value because of consideration only of the diminished earnings during the period of national receding economy and depression?

REASONS RELIED ON FOR THE ISSUANCE OF A WRIT OF CERTIORARI.

1. The Circuit Court of Appeals has decided an important question of Federal law which has not been, but should be, settled by this court, namely, whether a plan promulgated by the Interstate Commerce Commission can be sustained as equitable which completely excludes the stockholders of the Debtor from participation therein although complete solvency now exists by a wide margin.

2. The Circuit Court of Appeals has decided an important question of Federal law which has not been, but should be, settled by this court, namely, whether a plan promulgated by the Interstate Commerce Commission can be sustained as equitable which completely excludes stockholders of the Debtor from participation therein, the plan having been formulated on the basis of pre-war peacetime earnings when the established post-war peacetime earnings are greatly in excess thereof, being from one to six times the annual amounts thereof.

3. The Circuit Court of Appeals has decided a Federal question in a way probably in conflict with applicable

decisions of this court. The decision of the Court of Appeals excluding the stockholders of the Debtor from participation in the reorganization in the face of undenied solvency of the Debtor and in the face of unquestioned post-war peacetime earnings greatly in excess of the pre-war peacetime earnings upon which the reorganization was predicated, is probably in conflict with the following decisions of this court:

Ecker v. Western Pacific R. Co., 318 U. S. 448, 87 L. Ed. 892;
Group of Investors v. Milwaukee R. Co., 318 U. S. 523, 87 L. Ed. 959;
R. F. C. v. Denver & Rio Grande Western R. R. Co., 90 L. Ed. 1134.

4. The Circuit Court of Appeals has decided a Federal question in a way probably in conflict with the applicable decisions of this court, in sustaining a plan of reorganization which completely excludes stockholders from participation therein and thereby deprives them of their property without due process of law in contravention of the provisions of Amendment V to the Constitution of the United States. The applicable decisions are:

Group of Investors v. Milwaukee R. Co., 318 U. S. 523, 87 L. Ed. 959;
Kuehner v. Irving Trust Company, 299 U. S. 445, 81 L. Ed. 340;
Louisville Joint Stock Land Bank v. Radford, 295 U. S. 555, 79 L. Ed. 1593.

5. The Circuit Court of Appeals has rendered a decision in conflict with the decision of another Circuit Court of Appeals on the same matter, namely, the decision of the Circuit Court of Appeals for the Second Circuit in the case of **Adelaide H. Knight and William P. Doyle v. Wertheim & Co., et al.** (Decided December 31, 1946: Docket No.

20349). That case, a corporate reorganization under Chapter X of the Bankruptcy Act, came to the Court of Appeals on appeal from an order of the District Court denying a motion to amend a plan of reorganization after confirmation. The Court of Appeals reversed the District Court because of the unforseen changed financial conditions occurring after the confirmation. It held that the protection of the existing equities was more important than speed in the reorganization, and further that these equities belong to the stockholders and not to the other security holders. (Said opinion is attached hereto as Appendix D.)

PRAYER.

For the foregoing reasons, which are developed in further detail in the accompanying brief, your Petitioner prays that a writ of certiorari issue out of this Court to the United States Circuit Court of Appeals for the Eighth Circuit commanding said court to certify and send to this court on a day to be determined, a full and complete transcript of the record of all of the proceedings of such Court had in this cause, to the end that this case may be reviewed and determined by this Court; that the final order and decree of the said United States Circuit Court of Appeals be reversed, and that this Petitioner be granted such other and further relief as is proper.

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Railway Company, a corporation,
Debtor, Petitioner.

IN THE

SUPREME COURT OF THE UNITED STATES.

OCTOBER TERM, 1946.

ST. LOUIS SOUTHWESTERN RAILWAY COMPANY,
a Corporation, Debtor,
Petitioner,

vs.

BERRYMAN HENWOOD, as Trustee of ST. LOUIS SOUTHWESTERN RAILWAY COMPANY LINES, et al.,
Respondents.

BRIEF

In Support of Petition for a Writ of Certiorari to the United States Circuit Court of Appeals for the Eighth Circuit.

OPINIONS BELOW.

The opinion of the United States District Court for the Eastern District of Missouri (R. 5183-5213) is reported in 53 Fed. Supp. 914. The opinion of the United States Circuit Court of Appeals (R. 5559-5683) is reported at 157 Fed. (2d) 337.

JURISDICTION.

The final judgment of the Circuit Court of Appeals was entered August 26, 1946 (R. 5681). On September 9, 1946, the court issued an order extending to September 25, 1946 the time for filing petitions for rehearing, which time would otherwise have expired September 10, 1946 (R. 5683, 5684). Petitioner filed a petition for rehearing on September 25, 1946 (R. 5710). This petition was denied by the Court of Appeals October 22, 1946 (R. 5831).

Jurisdiction of this court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925 [28 U. S. C. Sec. 347 (a)] and under Section 24 of the Bankruptcy Act, as amended June 22, 1938 (11 U. S. C. Sec. 47).

This court's jurisdiction is supported by the following cases:

Ecker v. Western Pacific R. Corp., 318 U. S. 448, 87 L. Ed. 892;
Group of Investors v. Milwaukee R. Co., 318 U. S. 523, 87 L. Ed. 959;
R. F. C. v. Denver & Rio Grande Western R. R. Co., 90 L. Ed. 1134.

STATEMENT.

For the sake of brevity we refer to the Summary Statement of the Matter Involved, contained in the petition.

CONSTITUTIONAL PROVISIONS AND STATUTES INVOLVED.

Constitution of the United States of America, Amendment V:

> "No person shall be held to answer for a capital or otherwise infamous crime unless on a presentment or indictment of a grand jury, except in cases arising in the land or naval forces, or in the militia, when in actual service in time of war or public danger; nor shall any person be subject for the same offense to be twice put in jeopardy of life or limb; nor shall be compelled in any criminal case to be a witness against himself, nor be deprived of life, liberty or property without due process of law; nor shall private property be taken for public use without just compensation."

Section 77 (c) of the Bankruptcy Act is here involved. Because of its length, it is reproduced as Appendix E hereto.

SPECIFICATION OF ERRORS TO BE URGED.

The Circuit Court of Appeals erred:

I. In holding the reorganization plan of the Interstate Commerce Commission to be equitable although said plan excluded Debtor's stockholders entirely from participation therein, when, in the interim between the plan's approval by the Commission and the decision, the Debtor had ceased to be insolvent and has become solvent by a wide margin.

II. In holding the reorganization plan of the Interstate Commerce Commission to be equitable, even though it excluded the Debtor's stockholders from participation therein, when the plan was formulated on the theory that the Debtor's post-war peacetime earnings would not exceed Debtor's pre-war peacetime earnings, even though at the time of the decision by the Court of Appeals these earnings were proven to be much greater.

III. In ignoring the provisions of Amendment V to the Constitution of the United States, which provide that no person shall be deprived of property without due process of law and that private property shall not be taken for public use without just compensation, by sustaining a plan of reorganization which completely excludes stockholders from participation therein at a time when the unquestioned records of Debtor show that such stockholders have a very definite equity in the corporation.

SUMMARY OF ARGUMENT.

The argument will follow the foregoing specifications of errors to be urged.

ARGUMENT.

I.

The Circuit Court of Appeals Erred in Holding the Reorganization Plan of the Interstate Commerce Commission to Be Equitable Although Said Plan Excluded Debtor's Stockholders Entirely From Participation Therein, When, in the Interim Between the Plan's Approval by the Commission and the Decision, the Debtor Had Ceased to Be Insolvent and Has Become Solvent by a Wide Margin.

For the purposes of this writ, Petitioner will not question the correctness of the plan formulated by the Interstate Commerce Commission based on the evidence before it at that time. The Debtor had filed its petition for reorganization on December 12, 1935. The Commission had commenced hearings and had concluded them on April 24, 1937. On January 10, 1939, it reopened the hearings and did not conclude them until September 30, 1939. The final submission before the Commission was October 3, 1940. On June 30, 1941, the Report and Order of the Interstate Commerce Commission was filed (249 I. C. C. 5). Thereafter, on March 9, 1942, a modified Report and Order of the Interstate Commerce Commission was filed (252 I. C. C. 325). The plan of reorganization, therefore, which the Interstate Commerce Commission formulated was predicated entirely upon the figures of the period ending not later than December 31, 1941. Obviously the full effect of the tremendously increased war earnings had not yet been felt because Pearl Harbor Day had been only three weeks prior thereto.

Subsequent thereto, the Debtor has made great improvements in its financial position, it has accumulated

net current assets of $22,090,504, it has a total surplus of $35,354,529.79, and it has passed from a position of insolvency to a position of unquestioned solvency by an unquestionable margin.

Under the circumstances, the plan as formulated by the Commission and as sustained by the District Court and by the Circuit Court of Appeals has become grossly inequitable and cannot in good conscience be sustained.

This court has had before it in recent years three cases involving railroad reorganization, towit: **Ecker v. Western Pacific R. Corp.**, 318 U. S. 448, 87 L. Ed. 892; **Group of Investors v. Milwaukee R. Co.**, 318 U. S. 523, 87 L. Ed. 959; **R. F. C. v. Denver & Rio Grande Western R. R. Co.**, 90 L. Ed. 1134. In each of these cases, the Supreme Court has taken cognizance of the fact that a change in financial conditions subsequent to the formulation of a plan might render the plan inequitable.

In the case of **Ecker v. Western Pacific R. Corp.**, 318 U. S. 448, 87 L. Ed. 892, the Court said, l. c. 507, 949:

> "Respondents ask us to take into consideration the changed conditions since the Commission acted."

The Court then proceeded to consider the changed conditions without questioning in any respect the propriety of doing so. By stipulation of the parties, reports of operating results, combined, had been filed for the period from December, 1938, to July, 1942. The case was argued in the Supreme Court October 13, 1942. Quoting further, l. c. 508, 950:

> "In the interest of advancing the solution of as many problems in reorganization as possible, we have deliberated upon the effect to be given these unexpectedly large earnings. * * * Already serious proposals for decrease of tariffs have been advanced.

> • • • The Commission's forecast was made with knowledge of and not in disregard of past fluctuations of income, in war and in peace. On the showing as to changed conditions made before the District Court, there was no basis for a disapproval of the Commission plan as unfair to junior equities. The further evidence of increased earnings, placed in the record by the stipulations, does not lead us to reject the Commission's plan."

In **Group of Investors v. Milwaukee R. Co.**, 318 U. S. 523, 87 L. Ed. 959, the court stated, l. c. 542, 995:

> "The question of the increase in earnings since the Commission approved the plan raises of course different issues. As we have indicated in the Western R. Corp. Case, the power of the District Court to receive additional evidence may aid it in determining whether changed circumstances require that the plan be referred back to the Commission for reconsideration. • • •".
>
> "We agree with the Circuit Court of Appeals that no sufficient showing of changed circumstances has been made which requires the District Court to return the plan to the Commission for reconsideration. • • •".

L. c. 544, 996:

> "In view of these considerations we cannot say that the junior interests have carried the burden which they properly have of showing that subsequent events made necessary a rejection of the Commission's plan."

In the latest pronouncement upon this problem in the case of **R. F. C. v. Denver & Rio Grande Western R. R. Co.**, 90 L. Ed. 1134, this court said, l. c. 1143:

> "Changes in economic conditions cannot affect the powers of the reorganization agencies even though such changes may require a reexamination into the present fairness of the former exercise of these powers."

Again, l. c. 1148, the court said:

> "Assuming that the courts, as courts with equity powers in a bankruptcy matter, might set aside a plan, fair and equitable when adopted by the Commission, merely on account of subsequent changes in economic conditions of the region or the Nation, it should not be done when the changes are of the kind that were envisaged and considered by the Commission in its deliberations upon or explanation of the plan."

L. c. 1155:

> "Of course, this does not mean that if a plan is approved as fair and equitable by the Commission and the court, there cannot be a reasonable justification for its rejection by a class of claimants on submissions. **Reasons to make their objection reasonable may arise thereafter. For example, unanticipated, large earnings, might develop.**" (Emphasis supplied.)

It is thus obvious that this court has not in any of its railroad reorganization cases doubted for a moment the propriety of considering changed circumstances arising after the formulation and submission of the plan of reorganization.

This disposition of the Supreme Court is entirely consistent with its holdings in similar previous situations. In the case of **Central Kentucky Natural Gas Company v. Railroad Commission of Kentucky et al.**, 290 U. S. 264, 78 L. Ed. 307, the District Court had denied an injunction against rates prescribed by the State Railroad Commission for the sale of natural gas, which rates had been found to be confiscatory, because of plaintiff's failure to conform to a condition prescribed by the court as a prerequisite to the granting of the injunction. The rate was based upon a valuation as of December 31, 1926, although the case was not ready for a final decree until

September, 1932. The court mentioned some items of additional cost to plaintiff since that time and said, l. c. 274, 314:

> "That restriction also necessarily excluded from consideration the profound change in values, costs of service, consumption of commodities and reasonable return on invested capital which we judicially know took place during the period of more than five years while the case was pending before the Commission and the court. It is apparent that any decree, to be entered here, upon findings so restricted, must be similarly restricted in its operation and should speak of the validity of the Commission's rate only as of a time approximating the date when the franchise became effective. * * * The decree will state * * * that it makes no adjudication of the validity of the forty-five cent rate fixed by the Commission, so far as it may be affected by changed conditions after February 27, 1927, the effective date of appellant's franchise."

A similar instance of the consideration given by this court to changed conditions is found in the case of **A. T. & S. F. Railway Company et al. v. U. S., I. C. C., et al.**, 248 U. S. 248, 76 L. Ed. 273. Plaintiffs appealed from an order of the District Court denying the application for an interlocutory injunction against the enforcement of a rate order of the Interstate Commerce Commission. The record had been closed September 22, 1928. The matter had been submitted July 1, 1929. The order of the Interstate Commerce Commission was entered July 1, 1930. On February 18, 1931, the second petition for rehearing based upon economic changes was sustained and the order was amended April 10, 1931. This court there said, l. c. 260, 280:

> "It [the second petition for rehearing] was of the nature of a supplemental bill. It presented a new situation, a radically different one, which had super-

vened since the record before the Commission had been closed in September, 1928. * * *

"There can be no question as to the change of conditions upon which the new hearing was asked. Of that change we may take judicial notice. It is the outstanding contemporary fact, dominating thought and action throughout the country.

"It is plain that a record which was closed in September, 1928, relating to rates on a major description of the traffic of the carriers in a vast territory cannot be regarded as representative of the conditions existing in 1931. That record pertains to a different economical era and furnishes no adequate criterion of present requirements.

"In justification of this course [referring to the action of the Interstate Commerce Commission] it is urged on behalf of the Commission that its determination had been reached after regularly conducted and protracted hearings in which carriers and shippers had cooperated * * * and that a reopening would have meant further lengthy proceedings. It is said that 'in performing its legislative function of prescribing reasonable rates, the Commission necessarily projects into the future the results of a decision based on the conditions disclosed in the record' and that its determination 'cannot reflect accurately fluctuating conditions'. These suggestions would be appropriate in relation to ordinary applications for rehearing, but are without force when overruling economic forces have made the record before the Commission irresponsive to present conditions. This is not the usual case of possible fluctuating conditions but of a changed economic level and the prospect that a hearing may be long does not justify its denial if it is required by the essential demands of justice."

The cause was remanded to the District Court with directions to grant the injunction as prayed.

The language of the last quoted case is especially applicable to the instant problem. In connection with the finan-

cial condition of the Debtor now as compared with its condition at the time of the promulgation of the Commission's plan, we are not dealing with a mildly fluctuating condition **but with a definitely changed economic level.** This applies equally to the Debtor and to economic conditions generally in the region in which the Debtor operates. **The Debtor has passed from insolvency to solvency.** The post-war peacetime earnings are considerably higher than the pre-war peacetime earnings and the economic developments in the territories served by Debtor, coupled with the increased authorized freight rates, are bound to establish new economic peacetime levels for Debtor never before known.

As set out by Petitioner heretofore in its petition for the writ of certiorari, one very definite reason for this court granting the writ as prayed is that a question of Federal law, vitally important to the issues in the administration of railroad reorganizations under Section 77, is presented which has not been, but should be, settled by this court, namely, can a plan excluding stockholders be sustained as equitable **where the Debtor is solvent?**

In none of the other cases considered by this court, i. e., the **Western Pacific**, the **Milwaukee** and the **Denver & Rio Grande Western** cases, supra, has a situation been presented even remotely approaching the present problem. None of these roads was solvent at the time of the decision.

In the case of **Ecker v. Western Pacific R. Corp.**, supra, the petition for reorganization was filed in August, 1935. The Interstate Commerce Commission certified its plan in September of 1939. The District Court approved the plan; this court reversed the Circuit Court of Appeals in its reversal of the District Court. The stockholders of the Debtor were completely eliminated in the reorganization on the basis of the finding of the Commission that the stock

was valueless. There was no point made, and the record clearly showed that no point could be made, of any alleged solvency of the Debtor corporation. The language of the court indicated that there was actual bankruptcy and therefore the denial of any participation to the stockholders was justified. The following language appears in the opinion, l. c. 475, 933:

> "Assuming at this point that the Commission's valuation is sound and reached by allowable methods, a matter discussed later in this opinion, we hold that the elimination of the claims of stockholders and creditors which are valueless from participation in the reorganizations is in accordance with the valid provisions of Section 77 (e). **Actual bankruptcy** means a loss to some investors. Subsection (e) recognizes this inevitable result and provides a method for their elimination from the reorganization proceedings." (Emphasis supplied.)

Here, however, where there is no "actual bankruptcy," but the opposite, the investors should not be called upon to suffer a loss.

In the **Ecker** case this court indicates clearly the emphasis which it places upon the rights of stockholders. It says, l. c. 477, 934:

> "Stock which has no retirement provisions is the backbone of a corporate structure."

One of the cardinal considerations in a reorganization of a debtor railroad is the welfare of the public. This court has said that it is important that the stock of a properly reorganized railroad should have value and should enjoy the confidence of the nation. It is submitted by Petitioner that it would be exceptionally harmful to the position hereafter to be enjoyed by the nation's carriers if, in the face of absolute and unquestioned solvency, and clear and unquestionable stock values, as here presented, these values

can be completely wiped out by the affirmance of an arbitrary reorganization plan.

The second railroad reorganization case decided by this court is that of **Group of Investors v. Milwaukee R. Co.**, 318 U. S. 523, 87 L. Ed. 959. In that case the petition was filed in 1935 and the hearings were closed before the Interstate Commerce Commission in 1938. The Commission approved a plan in 1940. The District Court, after a hearing upon this plan, approved it in 1940, having before it the figures for the first half of the year 1940. The Circuit Court of Appeals reversed the District Court on the ground that the Commission had not made the findings required by the DuBois case[3] as to values. The reorganization plan in this case also eliminated the stockholders. Mr. Justice Douglas, in his opinion, l. c. 541, 995, made the following statement:

> "The finding of the Commission affirmed by the District Court under Section 77 (e) that the stock had no value is supported by evidence. The issue involved in such a determination is whether there is a reasonable probability that the earning power of the road will be sufficient to pay prior claims of interest and principal and leave some surplus for the service of the stock."

On the subject of the changed conditions since the formulation of the plan, the court says, l. c. 543, 995:

> "Late in 1939 the Commission had occasion to say, 'We know from past experience that the upswing in business which war brings is temporary and likely to be followed by an aftermath in which conditions may be worse than before.'"

The court then made reference to the Milwaukee's net operating income in the light of the last World War. These

3 Consolidated Rock Products Co. v. DuBois, 312 U. S. 510, 85 L. Ed. 982.

figures were as follows: 1916, $31,000,000; 1917, $21,500,000; 1918, $4,000,000; 1919, $2,000,000; 1920, more than a $14,000,000 deficit.

In a great many ways this last mentioned case is distinguishable from the instant case. First, there was no contention made and no possibility of contending that the Milwaukee Railroad was solvent. Second, there was no showing and no contention made that there was a "reasonable probability" that the earning power of the road would be "sufficient to pay prior claims of interest and principal and leave anything for the servicing of the stock." Third, the history of the Milwaukee road after the last war was decidedly different from that of the Cotton Belt. The comparable net railway operating income for the Cotton Belt (R. 5657) was as follows: 1917, $6,327,552; 1918, $3,320,342; 1919, $1,516,841; 1920, $4,511,938. The Cotton Belt continued at figures ranging from a high of $5,630,285 in 1923 to a low of $2,219,328 until 1932, when it showed a $196,791 deficit.

The third and most recent railroad reorganization case decided by this court is that of **R. F. C. v. Denver & Rio Grande Western R. R. Co.**, 90 L. Ed. 1134. In that case the petition for reorganization was filed in November of 1935, and it was not until June of 1943 that the Interstate Commerce Commission approved a plan. After one class of creditors had rejected it, the District Court affirmed the plan in October of 1943, holding that the rejection was not reasonably justified. In that case the creditors with secured claims against the reorganized roads were left undisturbed or allocated new securities of the new company. The plan completely eliminated unsecured claims and stockholders. The reversal by the Circuit Court was on the basis that the general bondholders were reasonably justified in rejecting the plan because the free cash in excess of operating capital needs and large earnings from war

business after the date of the plan, should be for the benefit of the general bondholders.

In that case the court, in commenting upon the power of Congress to authorize the Interstate Commerce Commission to eliminate valueless claims, said, l. c. 1041:

> "Liquidation in depression periods meant that large portions of debt, as well as stock interests in the properties would be irretrievably lost to their holders, while reorganization on a capitalization estimated what normal income would support meant the salvage of sound values."

Certainly if Congress was attempting to eliminate the unnecessary hardship attendant upon liquidation in depression periods, it was also the intent of Congress that the reorganization be made on the basis of normal earnings and not earnings of the depression period. To consider only the depression earnings, as the Circuit Court of Appeals did in the instant case, is in effect to give the stockholders no more than if the liquidation had been carried out in 1935 when the petition for reorganization was filed. This is exceptionally objectionable in view of the presently existing solvency of the Debtor road.

The **Rio Grande** case is clearly distinguishable from the instant case in many respects. In the first place, the condition of the Rio Grande made no near approach to solvency, whereas the Cotton Belt has become solvent by approximately $16,400,000. In the second place, the plan in the Rio Grande case was not formulated until June of 1943, after more than a year and a half of actual wartime operations, so that the Interstate Commerce Commission clearly had before it the figures of increased earnings and bettered cash position; in the Cotton Belt case the plan was formulated in March of 1942, only a few months after the commencement of hostilities. The fact that the Su-

preme Court considered this point in the **Rio Grande** case is demonstrated by that portion of its opinion hereinafter quoted, l. c. 1145:

> "We note also the contention that the possibility of a National income much higher and interest rates much lower than before World War II would affect valuation based on prospective earnings. Those factors, we think, were before the Commission when it made its earnings estimate."

In all of these decisions this court has pointed out that the reorganization plans cannot be made on the basis of any rigid mathematical formula, but must represent the best judgment of the Interstate Commerce Commission based upon its qualified and thorough investigation. The court has indicated that it is its function to keep the plans of the Commission within legal limits. That means that the Commission's plans may not be so conservative as to be inequitable under Section 77. The Commission is not called upon to formulate a plan which is absolutely and under all circumstances foolproof. A very pertinent statement to this effect is made by this court in the **Rio Grande** case, l. c. 1155:

> "These respondents cannot be called upon to sacrifice their property so that a depression-proof railroad system might be created."

The St. Louis Southwestern Railway Company, Debtor, is unquestionably solvent today. Its stock has a very real and substantial value. It is helpful to re-examine the provisions of Section 77 to determine whether under these circumstances a plan may be upheld which ignores and destroys these values.

Subsection (b) of Section 77 places a limit upon fixed charges as follows:

> "(b) A plan of reorganization * * * (4) shall provide for fixed charges * * * in such an amount that, after due consideration of the probable prospective earnings of the property in the light of its earnings experience and all other relevant facts, there shall be adequate coverage of such fixed charges by the probable earnings available for the payment thereof."

There is no positive direction in this section to destroy the rights of stockholders; that is left to the discretion of the Commission, subject to legal limitations. The only mandate of the statute relates to the fixed charges; and there again no guarantee of infallibility is exacted of the Commission. The Commission is directed to consider the "probable" prospective earnings of the property, not the "minimum possible" earnings of the property. The "probable prospective earnings" are to be determined in the light of both the "earnings experience" and "all other relevant facts." Certainly the earnings experience of the Debtor Railroad justifies consideration of stockholders in the reorganization plan. The term "all other relevant facts" would certainly include a consideration of the solvency of the Debtor Road.

By Subsection (e) of Section 77, the District Court must be satisfied that the plan is "fair and equitable"; that it "affords due recognition to the rights of each class of creditors and stockholders"; that it "does not discriminate unfairly in favor of any class of creditors or stockholders"; and that it "will conform to the requirements of the law of the land regarding the participation of various classes of creditors and stockholders."

Can a plan be said to be "fair and equitable" which deprives stockholders of their clear and established rights? Can a plan be said to "afford due recognition to the rights of each class of stockholders" which destroys

rather than recognizes these rights? Can a plan be said "not to discriminate in favor of any class of creditors" when in the reorganization it completely excludes definite values and in effect transfers these values to creditors already amply provided for? And finally, can a plan be said "to conform to the requirements of the law of the land regarding the participation of the various classes of creditors and stockholders," which violates the laws of the land by destroying those rights?

In Subsection (e) of said Section 77 the following direction is given with regard to the ascertainment of value:

> "The value of any property used in a railroad operation shall be determined on a basis which will give due consideration to the earning power of the property past, present and prospective, and all other relevant facts. In determining such value only such effect should be given to the present cost of reproduction new and less depreciation and original cost of the property, and the actual investment therein, as may be required under the law of the land, in light of its earning power and all other relevant facts."

It is significant that the word "power" appears in connection with the word "earning." In other words, the value of the railroad is not to be determined upon the basis of earnings, but on the basis of the potentialities of earnings. In the case of a utility whose rates are controlled by regulation, its earning power might be and often is considerably in excess of its actual earnings at any given time.

Moreover, the earning power which must be considered in determining value, according to the letter of the statute, is the "past, present and prospective" earning power. However, in the instant case the Circuit Court of Appeals would ignore the present earning power and the earning power for all of the war years entirely, brushing it aside

as unimportant, in clear violation of the express mandate of the statute. The Circuit Court of Appeals would ignore the prospective earning power of the Debtor Railroad in the light of changed economic and financial conditions and would interpret everything in the light of the unfortunate years of the depression era.

Furthermore, this "value" must, according to the statute, give consideration not only to the earning power of the property, but to "all other relevant facts." What could be more relevant than the supervening solvency of the Debtor corporation?

The effect of the decision of the Court of Appeals would be the same as to say that a man apparently dead who, while being prepared for burial, demonstrates clearly that he is alive, must nevertheless be buried because of the "irrelevancy" of his being alive.

As was pointed out in the petition for certiorari, the Debtor Road was found by the Commission to be insolvent by the amount of $8,304,118 based on the figures of December 31, 1941. Based upon the figures of the Commission and the undeniable statistics of the subsequent operations of the Debtor, the Debtor is now solvent by approximately $16,400,000. The present balance of assets over liabilities may be used, as Debtor has in fact used them, to pay off the principal of existing indebtedness so that future net income will not be subject to the payment of the interest charges thereon. On the other hand, these earnings may be put back into the system in the form of improvements in service, efficiency and equipment so that future revenue will be augmented. These facts become very pertinent in view of the emphasis placed by this court in its decisions upon earning power of debtor roads. The Court of Appeals, however, in its opinion seems to ignore this situation.

As indicated in the petition, Debtor has paid off $10,623,251 of principal and interest which was funded in the plan. The Commission in its supplemental Order (R. 3790) provided that the $75,000,000 capitalization is "subject to variation to the extent, if any, that matured interest proposed to be funded in the plan is paid * * * and as equipment obligations or other liabilities are paid or reduced." This would indicate that the total capitalization of Debtor is to be reduced by such amounts which would leave the capitalization at approximately $64,375,000 without regard to the increase of $11,768,354 in road and equipment property. This would give even greater force to the claims of the stockholders that the plan eliminating them is most inequitable.

In the petition the Debtor pointed out the substantial increase in the account of its property devoted to railway service (p. 12). This showed an increase in road and equipment property from December 31, 1941 (the latest date the Commission could have had in mind in formulating its modified plan) to October 31, 1946 (the last figures available) from $124,808,960 to $136,577,300, an increase of $11,768,354. Certainly these increases in investment in road and equipment are proper additions to the improvement in the financial position of the Debtor for the dates in question.

The petition also pointed out (p. 9) that the Debtor's current financial position (debt, interest and net current assets) has improved by $24,702,942 between December 31, 1941 and October 31, 1946, and is presently improving at the rate of $6,000,000 per year.

The intention of Congress in these matters is demonstrated by the passage at the last session of Congress of the so-called Wheeler-Reed Bill (S. 1253). Under this legislation the then existing reorganiaztion plans for railroads

would have been rejected and the Debtors would have been allowed an eighteen-months period to effect an agreement upon their plans of reorganization with the various interests involved. President Truman vetoed the Bill but indicated in his message that the aim of the legislation, to prevent forfeiture of railroad securities in reorganization proceedings, met with his approval. There seems to be no doubt but that similar legislation will be introduced in the present session of Congress. The case of the Cotton Belt was frequently mentioned throughout the legislative hearings on this Bill as the outstanding case on the issue of the inequity of eliminating junior interests. There was a great deal of public pressure behind this legislation for the reason that it was felt inequitable that stockholder interests should be eliminated in spite of intervening greatly improved financial conditions.

Senator Wheeler, Chairman of the Senate Committee on Interstate Commerce, and one of the sponsors of the legislation, made the following statement:

> "If you had not had these changed conditions there would not have been this complaint we have from all the country, from stockholders and bondholders and everybody else. I just don't believe that the Commission ought to hesitate at all to say that in view of the changed conditions there ought to be some changes."[4]

President Truman wrote in his Memorandum of Disapprovement, dated August 13, 1946:

> "By withholding my signature to this bill I do not intend to indicate that I favor the pending reorganization plans. I am in agreement with those objectives of the bill which prevent undesirable control of the railroads, either immediately or within a few years, and which prevent forfeitures of securities."

[4] Hearings before the Senate Committee on Interstate Commerce on S. 253 (79th Congress, 2nd Session, Page 412).

The Circuit Court of Appeals based its opinion in this case, in part, upon a mistaken interpretation of the records. The court held (R. 5663-5664) that it appeared "that the total long-term debt has increased, as to principal, comparing January 1, 1938 ($70,045,250) with December 31, 1944 ($75,725,439), by the sum of $5,680,189." In so holding the court overlooked a material matter of fact, that is, the figure of $75,725,439 appearing on page 5261 of the printed record includes the Second Mortgage Bonds in the sum of $10,000,000 without deduction of $6,957,500 of these bonds owned by the Debtor (R. 5259), and also includes open accounts with Debtor's wholly-owned subsidiaries, Southwestern Transportation Company and the Southwestern Town Lot Corporation of $890,290 and $11,516, respectively (R. 5261). When these figures are taken into account, the principal of the long-term indebtedness of the Debtor between January 1, 1938 and December 31, 1944, has not increased in the sum of $5,680,189 as stated in the court's opinion but has decreased in the sum of $2,719,116.

Another aspect wherein the opinion of the Circuit Court of Appeals was inadvertently based upon misinterpretation is found (R. 5668) in the following statement:

> "As to reduction in indebtedness, there is question. As to long-term debt, including interest in default and 'other deferred liabilities' (not important comparatively and showing little change) the comparative general balance sheet, for 1941 to 1944, inclusive, shows $85,025,067 for December 31, 1941, $85,344,703 for the same date, 1942, $82,840,465 for 1943 and $85,971,302 for 1944."

The court inadvertently overlooked a change in accounting required by the Interstate Commerce Commission as a result of which the notes of the Chase National Bank of the City of New York, of Mississippi Valley Trust Company, and of the Railroad Credit Corporation are classified

as current liabilities under "loans and bills payable (in default)" for the years 1941, 1942 and 1943, while the same obligations appear for 1944 under "long-term debt." This is shown in Debtor's statements at page 5261 of the printed record.

On Exhibit B attached to the Debtor's petition for rehearing were the details making up the totals in the above quotation to which were added for the years 1941, 1942 and 1943 "loans and bills payable (in default)" giving new totals. On Exhibit B the Second Mortgage Income Bonds were shown at $10,000,000 throughout, and in order to have consistent treatment of the figure of long-term debt, there has been deducted from the total of the long-term debt and overdue interest, $6,957,500 Second Mortgage Income Bonds in the treasury and the open accounts due from the wholly-owned subsidiaries, Southwestern Transportation Company and the Southwestern Town Lot Corporation. Thus the sum of the long-term debt and deferred liabilities for the end of the year 1941 was $82,753,529; for 1942, $82,675,256; for 1943, $80,172,851, and for 1944, $78,111,996. This results in a decrease from the years 1941 to 1944 of $4,641,533 instead of an increase from $85,025,067 in 1941 to $85,971,302 in 1944 as inadvertently stated in the opinion of the court.

One of the reasons assigned for the issuance of the writ in the Petition for Certiorari was that the Circuit Court of Appeals for the Eighth Circuit, in its opinion herein, was in conflict with the Circuit Court of Appeals for the Second Circuit as shown by the decision of said last-named court in the case of **Adelaide H. Knight and William P. Doyle v. Wertheim & Co. et al.** (Decided December 31, 1946: Docket No. 20349). That case involved an appeal from an order of the District Court refusing to submit to the creditors and the shareholders of the Debtor in a

reorganization proceeding under Chapter X of the Bankruptcy Act an "alteration" of a plan of reorganization. The Debtor was the owner of a large office building in New York. The Debtor had one class of capital stock, First Mortgage Bonds in the amount of $16,000,000, Second Mortgage Bonds in the amount of $3000 and 5% Debentures in the amount of $4,754,000. The plan provided that the First Mortgage Bonds should remain untouched, that the balance due on the Second Mortgage Bonds should be paid, that a new company should be formed to issue to the debenture holders convertible income bonds for 60% of their holdings as well as ten shares of new stock for every One Hundred Dollars; that the claims of the unsecured creditors should be paid in full in cash; that the old shareholders should receive shares in the ratio of one to ten. The new convertible income bonds were to be secured by a Second Mortgage and the bondholders had the right to convert them into new shares, within two years after issue, on the basis of sixteen for each one hundred dollars; and within three years after issue on the basis of ten shares for each one hundred dollars.

The petition for reorganization was filed April 10, 1941. The trustee filed the plan of reorganization February 24, 1944. By May 11, 1945 the plan had taken substantially its final form. On December 4, 1945, the court approved the plan. Notice was given to all creditors and shareholders affected and on May 13, 1946, the judge entered an order of confirmation. He signed various auxiliary orders during June and July and on July 8, 1946 entered an order of "consummation." Before the prescribed transfers had been made, two shareholders on July 11, 1946 filed the petition which is the basis of the appeal and which proposed as an "alteration" or "modification" of the plan, an offer of a large real estate company. This offer was to give the old shareholders an option to buy

the new company's shares at $4.50 a share; to underwrite the issue; to receive as a commission 69,686 shares; and with the money so raised, together with the debtor's liquid assets, to pay off the debentures, principal and interest. The option price was later raised to $5.50 and on July 19 to $6.00; the offer was to expire October 17, 1946. The District Court held extensive hearings at which the shareholders urged acceptance and the debenture holders opposed it, for the price of the bonds had risen far above the amount of the principal and interest. The district court denied the petition, using the following language in its memorandum:

> "The deliberate and fully considered adjudication of a responsible court made and entered without objection on the part of any person in interest—and after all parties were afforded ample opportunity to be heard on the merits of the issues involved—and when they and the public—as they had a right to do—confidently relied upon its integrity, should be something more stable than a weathervane. • • • For this reason, my consummation order of July 8, 1946 will stand. It follows that the application to reopen the organization proceedings of the Debtor will be denied."

The appellants argued that the appeal should be dismissed because the bankruptcy judge denied the motions, not for lack of power, but in his discretion and because the offer of the real estate company had expired. The Court of Appeals agreed that the bankruptcy judge had acted in his discretion and said:

> "Therefore, the order may not be disturbed unless he overstepped the permissible limits of his discretion."

The Court of Appeals also disposed of the point that the offer had expired. The court then took up these questions:

First, as to whether the judge had the power to submit the offer to the shareholders; the Court of Appeals held that he did. It traces the steps required by Chapter X, pointing out that the plan shall first have the "approval" of the judge after the hearing provided for by the statute; the parties interested must accept it at a second hearing after which it is ready for "consummation." It must then be performed, "consummated," and when "consummated," the judge must enter a "final decree" which discharges the Debtor from all its debts, cuts off the shareholders, and discharges the trustee. The court points out that the order of "consummation" is not conclusive. A significant quotation from the court's statement upon this point is as follows:

> "The plan, as confirmed, went back at least to December, 1945, and more properly to May, 1945, and the rise in value of the Debtor's property which prompted the offer of the City Investing Company could not have been then foreseen."

The next question considered by the Court of Appeals was whether the judge, having power to accept the "alteration" was free as a matter of discretion to reject it. Here the court said:

> "The only considerations which, so far as we can see, might properly have moved him to do so were (1) a conflict of interest between the debenture holders and the shareholders; (2) the fact that after long years of delay the reorganization had finally culminated in a confirmed plan, and (3) doubts that the new company would be too much stripped of liquid assets to keep afloat. These we shall take up seriatim. We cannot agree that the debenture holders had as yet any legally protected interest in the property beyond the principal and accrued interest of their bonds, which could be weighed against the shareholders' interest. If in fact they had relied upon

sharing in an equity in the property above that amount, it was without warrant of law and constituted no reason for depriving the shareholders of whatever chance might remain of realizing upon their property. * * * It is of course true that there must come a time when a mortgagee or a creditor, who takes over his Debtor's property in extinguishment of the debt, gets an indefeasible title, just as the mortgagee did in equity upon final decree of strict foreclosure; but Chapter X provides its own date when this shall occur; it is the date of the entry of the 'final decree' under Section 228. It is that decree which puts an end to 'all rights and interests of stockholders' and discharges all 'debts and liabilities' of the Debtor. Until then creditors remain creditors; they have their claims and that is all they have; any 'modification' which guarantees them principal and interest on those claims, secures all the rights that a court need regard. The offer of the City Investing Company of July 11, 1946 did that; and we answer the first question that there was no party to the reorganization whose interest the judge could properly weigh against that of the shareholders, except insofar as by further delay the debenture holders' claims might be imperiled.

"Next, as to that delay and as to the fact that the plan had been confirmed." * * *

"That does not indeed mean that delay in presenting an 'alteration' or 'modification' can never be relevant to its approval; we recognize the force of what the judge said in his opinion, which we have quoted, that the considered judgment of a court is not to be lightly put aside. But there can be considerations more imperative than the dispatch of judicial business, even after delays so long as existed in this case. If the legally protected interests of any opposing parties are fully preserved, it is not a good reason to deny others any reasonable chance to protect their own interests that they have been long in asserting them. Had it been shown that the equity which was presupposed in the proposal of the City Investing Company had existed for a substantial time before

> July 11, 1946, there would be force in what the judge said in his opinion; but that was not shown; so far as appears, the equity may have arisen from a recent increase in the value of the property. Delay would not cost the debenture holders anything, for the proposal would give them interest until payment upon the full face of their bonds instead of upon sixty per cent of it; and the property was adequate security."

The Court of Appeals held that the "alteration" should have been submitted and that it was error to deny the petition.

It is obvious that the decision of the Circuit Court of Appeals for the Eighth Circuit in the instant case is at variance with the above quoted opinion of the Circuit Court of Appeals for the Second Circuit. The Second Circuit has clearly stated that the unquestionable equities of the shareholders do not belong to the bondholders and may not be appropriated legally for them. The opinion clearly indicates that while expedition is desirable in the handling of reorganization matters, it is not to be sought at the cost of the legal rights of stockholders who have admitted equities.

As clearly indicated in the foregoing opinion of the Second Circuit, we have not reached the point in the reorganization of the Debtor Railroad where the plan of reorganization has become final and irrevocable. The mere fact that a plan has been approved by the District Court does not create any irrevocable establishment of rights. It is provided in Section 77 (e) [U. S. C. 205 (e)] that after the approval of the plan the judge shall certify his opinion and order to the Commission. The plan is then submitted by the Commission to the creditors and stockholders for acceptance or rejection as provided by law. Next the Interstate Commerce Commission certifies to the judge the results of such submission. Upon receipt of

such certification, the judge confirms the plan if satisfied that it has been accepted as required by law or that it is fair and equitable for the interests of those rejecting it. The District Judge then enters an order and files an opinion of confirmation.

In Section 77 (f) [U. S. C. Section 205 (f)] it is provided that upon confirmation by the judge the provisions of the plan shall (subject to the right of judicial review) be binding upon the debtor and all stockholders thereof and all creditors. Upon termination of the proceedings a final decree is entered discharging the trustee or trustees and making such provisions as may be equitable by way of injunction or otherwise and closing the case.

It is clear, therefore, that the security holders of the Debtor for whom provision has been made in the present plan of reorganization have no vested or irrevocable rights therein which may not be altered by any new plan necessary to do full justice to the stockholders of the Debtor as well as to other security holders.

II.

The Circuit Court of Appeals Erred in Holding the Reorganization Plan of the Interstate Commerce Commission to Be Equitable, Even Though It Excluded the Debtor's Stockholders From Participation Therein, When the Plan Was Formulated on the Theory That the Debtor's Post-War Peacetime Earnings Would Not Exceed Debtor's Pre-War Peacetime Earnings, Even Though at the Time of the Decision by the Court of Appeals These Earnings Were Proven to Be Much Greater.

The Circuit Court of Appeals in its opinion tended to ignore all questions except the question of earnings in passing upon the plan promulgated by the Commission.

In ignoring all factors other than earnings, it is respectfully submitted the Court of Appeals was in error.

As we have already pointed out, Subsection (b) of Section 77 directs the providing of fixed charges in such an amount that "after due consideration of the probable prospective earnings of the property in light of its earnings experience and all other relevant facts, there shall be adequate coverage of such fixed charges by the probable earnings available for the payment thereof." We have heretofore called attention to the fact that the earnings to be considered are not the "absolutely certain" earnings but the "probable prospective" earnings of the property. In determining these earnings, the Commission is enjoined to consider the "earnings experience" and "all other relevant facts." These relevant facts certainly include (1) the solvency of the Debtor Road, (2) the increase in rates allowed by the Interstate Commerce Commission, (3) the improvement in the system of the Debtor and (4) the greatly increased population and industry of the area served by the Debtor.

By Subsection (e) of Section 77, in determining value due consideration must be given to the earning power of the property, past, present, and prospective and all other relevant facts.

One element of future earning power of the Debtor which could not have been considered by the Court of Appeals and yet which has important bearing upon the problem, is the action of the Interstate Commerce Commission in its decision of December 5, 1946. In Ex Parte No. 162, Increased Railway Rates, Fares and Charges, 1946, and Ex Parte No. 148, Increased Railway Rates, Fares and Charges, 1942, the Commission permits increases of basic freight rates by twenty per cent for the future and permits continuation of previously granted passenger fare

increases. Certainly it cannot be denied that this greatly enhances the Debtor's permanent post-war earning power considerably beyond anything the Interstate Commerce Commission could have had in mind when it formulated its plan and beyond what the Circuit Court of Appeals could have had in mind when it looked out upon so pessimistic and dark a future.

This authorized rate increase shows that this Court's pessimism was unjustified in the **Ecker** case, supra, when it said, l. c. 508, 950: "Already serious proposals for decrease of tariffs have been advanced."

In its petition Debtor pointed out the marked and spectacular population growth in the area served by the Debtor Railroad and its connections. It is entirely possible that the war contributed to this increase but there is no indication whatsoever that the population shift has not become permanent. The population of Los Angeles increased in six years by twenty per cent from April, 1940 to January, 1946. Houston increased from 384,514 to 478,000, Dallas from 294,734 to 425,000 and Ft. Worth from 177,662 to 235,117. These increases occurred in the six years between 1940 and 1946. The total California and Texas population increases between April of 1940 and July of 1945 were 27.7 per cent and 5.8 per cent, respectively. During this same period the total population of the United States as a whole increased by only .2 per cent.

The business growth of these cities has been equally phenomenal.[5]

Even if we were entirely to ignore the other vitally important circumstances, nevertheless, on the basis of estab-

[5] The Monthly Business Review of the Federal Reserve Bank of Dallas, January 1, 1946, Volume 31, No. 1, pages 3-4, makes the following observation in an article captioned "Postwar Prosperity in the Southwest": "This regional area experienced a greatly accelerated industrial expansion and development during the war years, the rate of growth having been above the average rate of expansion for the country as a whole."

lished earnings alone the inequity of the proposed plan of reorganization is apparent. Appendix C to the petition shows the income available for fixed charges during the first ten months of operation during the year 1946 to be $5,949,631.47. Projecting this figure for the balance of the year, the annual income available for fixed charges will be approximately $7,000,000. This is greatly in excess of the pre-war peacetime earnings during any year considered by the Interstate Commerce Commission. It is from two to six times as large as the comparable figures for the pre-war period from 1930 to 1940. The Commission's plan (R. 3785) provides annual charges of $2,451,228 consisting of $1,513,723 interest and $937,505 for preferred stock dividends. The 1946 income available for fixed charges is, therefore, nearly three times the amount of these annual charges. Bearing in mind that the year 1946 represents peacetime earnings, this figure is highly significant.

The figure may also be considered an indication of Debtor's long-term future in view of the intervening industrial development and population growth as well as because of the action of the Interstate Commerce Commission above referred to in awarding the substantial rate increases. Certainly these earnings for the year 1946 cannot be cataloged in the Circuit Court's brusque fashion as "uncertain elements" or as elements which "can find no place in estimated future earnings for reorganization valuation purposes."

With these high peacetime earnings we have an element in the instant case which clearly and unequivocably distinguishes it from the **Milwaukee**, the **Western Pacific** or the **Denver & Rio Grande** cases heretofore considered by this court.

Moreover, upon reconsideration of its plan, lower interest rates could be justifiably provided for by the Com-

mission so that the same amount of net earnings hereafter could take care of the annual costs of a considerably higher capitalization than was the case when the Commission considered this capitalization.

III.

The Circuit Court of Appeals Erred in Ignoring the Provisions of Amendment V to the Constitution of the United States Which Provide That No Person Shall Be Deprived of Property Without Due Process of Law and That Private Property Shall Not Be Taken for Public Use Without Just Compensation, by Sustaining a Plan of Reorganization Which Completely Excludes Stockholders From Participation Therein at a Time When the Unquestioned Records of Debtor Show That Such Stockholders Have a Very Definite Equity in the Corporation.

The Bankruptcy Act itself and the adjudicated cases demonstrate clearly that the bankruptcy power is subject to the due process clause of Amendment V to the Federal Constitution. Section 77 (e) of the Bankruptcy Act [11 U. S. C. 205 (e)] expressly provides that the court shall give "due notice" to all parties in interest of the time within which such parties may file their objections to the plan. It provides that the judge shall "after notice" in such manner as he may determine to the Debtor, its trustee, stockholders, creditors, and the Commission "hear" all parties in interest. It provides that after such hearing, if objections are filed to the plan, the judge shall approve the plan if satisfied that it is "fair and equitable," does not "discriminate" unfairly in favor of any class of creditors or stockholders, and will conform to the requirements of the "law of the land." It provides that in determining value such effect shall be given to the present cost of reproduction new and less depreciation and the original

cost of the property, and the actual investment therein "as may be required under the law of the land," in light of its earning power and other relevant facts. All of these various terms, namely, "notice", "hearing", "fairness", "equity", "no unfair discrimination" and "law of the land" connote that "due process of law" as those words are employed in the Federal Constitution, is contemplated and required in the court's approval of a plan of reorganization.

The case of **Pennoyer v. Neff**, 95 U. S. 714, 24 L. Ed. 565, is a milestone on the subject of due process of law. Pertinent language appearing in this opinion, l. c. 732, 572, is as follows:

> "Whatever difficulty may be experienced in giving to those terms ["due process of law"] a definition which will embrace every permissible exertion of power affecting private rights, and exclude such as is forbidden, there can be no doubt of their meaning when applied to judicial proceedings. They then mean a course of legal proceedings according to those rules and principles which have been established in our systems of jurisprudence for the protection and enforcement of private rights."

To take existing valuable rights from the stockholders of the Debtor under the proposed plan of reorganization is clearly violative of the provisions of the Fifth Amendment to the United States Constitution.

This court recognized the point here made by Debtor in the case of **Louisville Joint Stock Land Bank v. Radford**, 295 U. S. 555, 79 L. Ed. 1593. Mr. Justice Brandeis there declared, l. c. 589, 1604:

> "The bankruptcy power, like the other great substantive powers of Congress, is subject to the Fifth Amendment. Under the bankruptcy power Congress may discharge the Debtor's personal obligations because, unlike the states, it is not prohibited from im-

pairing the obligation of contracts. * * * But the effect of the act here complained of is not the discharge of Radford's personal obligation. It is the taking of substantive rights in specific property acquired by the Bank prior to the Act."

And subsequently in the same case it was stated, l. c. 602, 1611:

"For the Fifth Amendment commands that, however great the Nation's need, private property shall not be thus taken even for a wholly public use without just compensation. If the public interest requires, and permits, the taking of property of individual mortgagees in order to relieve the necessities of individual mortgagors, resort must be had to proceedings by eminent domain; so that, through taxation, the burden of the relief afforded in the public interest may be borne by the public."

The last quoted section is particularly applicable to the facts of the instant case. No public emergency, however great, could constitutionally sanction the taking from the stockholders of the Debtor their established existing values without compliance with constitutional limitations.

The Bankruptcy Act, as amended, defines solvency in the following language [11 U. S. C. A., Sec. 1 (19)]:

"A person shall be deemed insolvent within the provisions of this title whenever the aggregate of his property, exclusive of any property which he may have conveyed, transferred, concealed, removed, or permitted to be concealed or removed, with intent to defraud, hinder, or delay his creditors, shall not at a fair valuation be sufficient in amount to pay his debts."

By these standards the Debtor corporation is unquestionably solvent at the present time by a clear margin.

An illuminating decision is that of the Circuit Court of Appeals for the Second Circuit in the case of **Meyer**

et al. v. Dolan et al., 145 Fed. (2d) 880 (Certiorari Denied, 65 S. Ct. 916, 89 L. Ed. 1422). This was an appeal from an order of the District Court for the Northern District of New York made after hearings on a plan of reorganization proposed by the trustee of a debtor in proceedings under Chapter X of the Bankruptcy Act. The court found that the debtor was insolvent and the order from which the appeal was taken was to the effect that its common stockholders had no interest to be protected in the reorganization proceedings. The court said, l. c. 881:

> "This is one of several plans for reorganization which have been proposed and which have failed of adoption for one reason or another, and the present issue is a rather narrow one. **Whether or not the debtor is insolvent and its common stock is, therefore, to be treated as worthless in proposing and considering a plan of reorganization depends, of course, upon whether the amount of its liabilities exceeds the fair market value of its assets.** 11 U. S. C. A. 1 (19). That is a question of fact which the judge below decided adversely to the appellant * * *." (Emphasis supplied.)

We are not here dealing with the right of Congress by appropriate legislation to impair the obligation of contracts. We are dealing with the question of the right, under Congressional enactments, to destroy a property interest.

This distinction is made in the case of **Kuehner v. Irving Trust Company**, 299 U. S. 455, 81 L. Ed. 340. This case dealt with the restriction in Section 77B (b) (10) of the Bankruptcy Act upon the claim of the landlord under a lease. The point was made that it actually offended the due process guarantee by destruction of rights conferred by the lease. Reference was made to the **Louisville Joint Stock Land Bank v. Radford** case, supra. This court said, l. c. 451-2, 345:

> "As pointed out in the case last cited there is, as respects the exertion of the bankruptcy power, a significant difference between a property interest and a contract, since the constitution does not forbid impairment of the obligation of the latter. The equitable distribution of the bankrupt's assets or the equitable adjustment of creditors' claims in respect of those assets, by way of reorganization, may therefore be regulated by a bankruptcy law which impairs the obligation of the debtor's contracts."

This court has always recognized the applicability of the provisions of the Fifth Amendment to railroad reorganizations. In the **Denver & Rio Grande Western Railroad Company Case**, supra, this court said, l. c. 1140-41:

> "(After speaking of the purposes of Congress in enacting Section 77) * * * the answer reached by Congress was that the experience and judgment of the Commission must be relied upon for final determinations of value and of matters affecting the public interest, subject to judicial review **to assure compliance with constitutional and statutory requirements.**" (Emphasis supplied.)

If, in fact, the Debtor at the time of the final order of reorganization is not insolvent the court would not be justified in approving any plan which excludes stockholders. The "due process" clause of the Fifth Amendment of the Federal Constitution protects the rights of all parties having an interest in the Debtor's property. No distinction can be made between stockholders and creditors in according "due process of law" in a reorganization proceeding.

It is therefore apparent that the proposed plan of the Commission under the existing circumstances violates the constitutional provisions contained in Amendment V.

CONCLUSION.

Wherefore, it is respectfully submitted that a writ of certiorari should issue as prayed.

Dated January 17, 1947.

JACOB M. LASHLY,
705 Olive Street,
St. Louis 1, Missouri,
Attorney for St. Louis Southwestern
Railway Company, a corporation,
Debtor, Petitioner.

(Appendices Follow.)

APPENDIX A.

APPENDIX A.

ST. LOUIS SOUTHWESTERN RAILWAY LINES

Long Term Debt; Interest in Default; and Net Current Assets as of Various Dates.

	December 31, 1941	December 31, 1943	December 31, 1944	December 31, 1945	July 31, 1946	October 31, 1946
Record reference	5259) 5261)	5259) 5261)	5259) 5261)	5694) 5696)	5694) 5696)	(Note)
Long Term Debt:						
First Mortgage Bonds	$20,950,000	$20,950,000	$20,950,000	$20,950,000	$20,950,000	$20,950,000
Equipment Trust Obligations	216,000	108,000	54,000	.....	.....	.....
Second Mortgage Bonds	3,042,500*	3,042,500*	3,042,500*	3,042,500*	3,042,500*	3,042,500*
First Terminal & Unifying Mortgage Bonds	8,063,000	8,063,000	8,063,000	8,063,000	8,063,000	8,063,000
General & Refunding Mortgage Bonds	9,327,500	9,327,500	9,327,500	9,327,500	9,327,500	9,327,500
Railroad Credit Corporation Note	#	#	557,989	421,940	382,249	.....
Chase National Bank Note	#	#	3,500,000	3,500,000	3,500,000	3,500,000
Mississippi Valley Trust Company Note	#	#	1,000,000	1,000,000	1,000,000	1,000,000
Reconstruction Finance Corporation Note (bought by Southern Pacific)	17,882,250	17,882,250	17,882,250	17,882,250	17,882,250	17,882,250
Texarkana Union Station Trust	315,000	315,000	315,000	315,000	315,000	315,000
First Mortgage Bonds in default	3,250,680	3,173,895	3,173,895	3,173,895	3,173,895	3,173,895
Loans & Bills Payable in default	5,658,469#	5,313,289#	.....#	.....#	.....#	.....#
Total Long Term Debt	$68,705,399	$68,175,434	$67,866,134	$67,676,085	$67,636,394	$67,254,145

Note: Figures for October 31, 1946 are taken from Appendix B to this petition.

* $10,000,000 outstanding, less $6,957,500 held in treasury.

\# Notes of the Railroad Credit Corp., Chase National Bank and Mississippi Valley Trust Co. were classified as "Loans and Bills Payable in Default" (a part of current liabilities) until January 1, 1944 when these debts were classified under "Long Term Debt" in accordance with Interstate Commerce Commission rules.

Interest in Default:						
Second Mortgage Bonds	$ 547,650	$ 60,850	$ 60,850	$	$	$ .....
First Terminal & Unifying Mortgage Bonds	2,418,900	1,411,025	403,150	201,575	33,596	134,383
General & Refunding Mortgage Bonds	3,031,437	3,124,713	3,031,438	2,575,063	1,904,365	2,020,958
Central Arkansas & Eastern Bonds	265,203	265,203	265,203	265,203	265,203	265,203
Stephenville North & South Texas Bonds	665,697	665,697	601,611	601,611	601,611	601,611
Reconstruction Finance Corporation	5,573,776	5,172,810	4,613,783	3,098,635	1,218,175	1,443,541
Others	1,360,160	1,236,485	1,080,458	670,764	167,971	225,130
Total Interest in Default	$13,862,823	$11,936,783	$10,056,493	$ 7,412,851	$ 4,190,921	$ 4,690,826
Total Current Assets	$10,883,688	$39,169,687	$43,566,776	$41,775,464	$34,285,775	$32,545,847
Total Current Liabilities less Loans & Bills Payable in default	2,872,875	25,729,597	29,389,479	20,535,069	13,809,181	10,455,343
Net Current Assets	$ 8,010,813	$13,440,090	$14,177,297	$21,240,395	$20,476,594	$22,090,504

APPENDIX B.

ST. LOUIS SOUTHWESTERN RAILWAY LINES
Berryman Henwood, Trustee
GENERAL BALANCE SHEET OCTOBER 31, 1946
ELIMINATING INTER-COMPANY ITEMS

ASSETS

Investments	Oct. 31, 1946
Road and equipment property	$136,538,870.45
Improvements on leased property	38,443.24
Less:	
Donations and grants	317,830.86
Accrued depreciation—Road	591,070.73
Accrued depreciation—Equipment	11,892,479.48
Accd. amort. of defense projects—Rd.	1,356,404.75
Accd. amort. of defense projects—Eq.	4,322,914.16
Net investment in Road & Equip.	118,096,613.71
Capital and other reserve funds	160,186.65
Miscellaneous physical property	275,368.28
Investments in affiliated companies:	
(A) Stocks	2,447,507.00
(B) Bonds	816,004.00
(C) Other secured obligations	7,376.27
(E) Investment advances	1,213,812.56
Other investments:	
(A) Stocks	54.48
(B) Bonds—Second Mortgage Income Bonds	6,957,500.00
(E) Advances	8,112.69
Total investments	129,982,535.64

Current Assets

Cash	1,281,303.54
Temporary cash investments	21,708,620.00
Special deposits	1,385,961.75
Traffic and car-service balance—Dr.	1,944,736.64
Net bal. receivable from agts. & conds.	468,468.81
Miscellaneous accounts receivable	1,499,962.53
Material and supplies	4,110,997.63
Interest and dividends receivable	16,800.00
Accrued accounts receivable	104,913.48
Other current assets	24,083.08
Total current assets	32,545,847.46

Deferred Assets

Working fund advances	39,476.49
Insurance and other funds	76 500.00
Other deferred assets	28,393.69
Total deferred assets	144,370.18

Unadjusted Debits

Prepayments	22,536.99
Other unadjusted debits	741,071.67
Total unadjusted debits	763,608.66
Grand Total	163,436,361.94

ST. LOUIS SOUTHWESTERN RAILWAY LINES
Berryman Henwood, Trustee
GENERAL BALANCE SHEET OCTOBER 31, 1946
ELIMINATING INTER-COMPANY ITEMS

LIABILITIES	Oct. 31, 1946
Capital stock—Common	$ 17,186,100.00
Preferred	19,893,600.00
Total stock	37,079,700.00
Long Term Debt	
Funded debt unmatured:	
First Mortgage Bonds	20,950,000.00
Second Mortgage Income Bonds	10,000,000.00
Texarkana Union Sta. Tr. Ctfs. Ser. "A"	315,000.00
Debt in default:	
First Mortgage Bonds	3,173,894.68
First Terminal & Unify. Mtg. Bonds	8,063,000.00
Gen. & Ref. Mtg. 5% Gold Bds. Series "A"	9,327,500.00
The Chase Natl. Bk. of the City of N. Y.	3,500,000.00
Mississippi Valley Trust Co.	1,000,000.00
Amounts payable to affiliated companies:	
Notes—RFC—Purchased by Sou. Pac. Co.	17,882,250.00
Open Accounts—Southwestern Transp. Co.	890,289.51
The S. W. Town Lot Corp.	20,444.97
Total long term debt	75,122,379.16
Current Liabilities	
Audited accounts and wages payable	1,814,177.14
Miscellaneous accounts payable	258,322.37
Interest matured unpaid	1,173,203.15
Unmatured interest accrued	63,170.82
Accrued accounts payable	58,711.50
Taxes accrued:	
State, county and city taxes	689,423.17
Federal income tax	6,021,755.77
Other federal taxes	126,348.24
Other current liabilities	249,730.76
Total current liabilities	10,455,342.92
Deferred Liabilities	
Interest in default:	
First Term. & Unify. Mtg. Bonds	134,383.33
Gen. & Ref. Mtg. 5% Gold Bds. Series "A"	2,020,958.33
Cent. Ark. and East. RR. Co. 1st Mtg. Bds.	265,202.93
S. N. & S. T. Ry. Co. First Mtg. Bonds	601,611.48
Reconstruction Finance Corporation	1,443,540.80
Others	225,130.41
Other deferred liabilities	199,620.04
Total deferred liabilities	4,890,447.32
Unadjusted Credits	
Other unadjusted credits	390,514.21
Accrued depreciation—Leased property	143,448.54
Total unadjusted credits	533,962.75
Surplus	
Earned surplus—Unappropriated	35,354,529.79
Total surplus	35,354,529.79
Grand Total	163,436,361.94

APPENDIX C.

ST. LOUIS SOUTHWESTERN RAILWAY LINES
Berryman Henwood, Trustee

INCOME ACCOUNT TEN MONTHS 1946

	January 1 to October 31, 1946
Railway Operating Revenues:	
Freight	$35,173,316.20
Passenger	1,571,517.14
Mail	259,914.08
Express	289,782.53
Miscellaneous transportation	240,709.29
Incidental	571,857.06
Joint facility (Net)	19,790.51
Total	38,126,886.81
Railway Operating Expenses:	
Maint. of Way & Structures	6,389,177.24
Maint. of Equipment	5,689,629.81
Traffic	1,196,526.14
Transportation	12,393,453.03
Miscellaneous Operations	372,011.68
General	1,127,437.17
Total	27,168,235.07
Net rev. from ry. oper's	10,958,651.74
Railway Tax Accruals:	
State, County & City taxes	831,222.58
Federal income tax	2,150,193.15
Fed. inc. tax—adj. 1941 & 1945	Cr. 403,095.39
Other federal taxes	1,196,315.93
Total	3,774,636.27
Railway operating income	7,184,015.47
Rent Income:	
Rent from locomotives	1,740.45
Rent from pass. train cars	25,001.26
Rent from work equipment	643.54
Joint facility rent income	281,135.79
Total	308,521.04
Rents Payable:	
Hire of frt. cars—Dr. bal.	995,685.83
Rent for locomotives	29.94
Rent for pass. train cars	84,012.86
Rent for work equipment	274.75
Joint facility rents	755,267.72
Total	1,835,271.10
Net rents—Debit	1,526,750.06
Net railway optg. income	5,657,265.41

Continued on next page

ST. LOUIS SOUTHWESTERN RAILWAY LINES
Berryman Henwood, Trustee

INCOME ACCOUNT TEN MONTHS 1946

	January 1 to October 31, 1946
Brought forward	$ 5,657,265.41
Other Income:	
Income from lease of rd. & equip.	8,362.60
Miscellaneous rent income	36,587.93
Miscl. nonoptg. phys. property	11,281.85
Income from funded securities	35,553.60
Income from unfd. sec. & accts.	218,617.93
Miscellaneous income	1,009.58
Total	311,413.49
Total income	5,968,678.90
Miscellaneous Deductions from Income:	
Miscellaneous rents	316.41
Miscellaneous tax accruals	656.26
Maint. of invest. organization	201.10
Miscl. income charges	17,873.66
Total	19,047.43
Inc. avail. for fixed chgs.	5,949,631.47
Fixed Charges:	
Rent for leased roads & equip.	11,248.18
Interest on funded debt (fixed)	2,483,068.37
Interest on unfunded debt	9,229.80
Total	2,503,546.35
Net income	3,446,085.12
Disposition of Net Income:	
Bal. of inc. transferred to Earned Surplus	3,446,085.12

APPENDIX D.

UNITED STATES CIRCUIT COURT OF APPEALS
For the Second Circuit.

No. 82—October Term, 1946.

(Argued November 11, 1946 Decided December 31, 1946.)

Docket No. 20349.

ADELAIDE H. KNIGHT, AND WILLIAM P. DOYLE,
Appellants,

v.

WERTHEIM & CO., ET AL.,
Appellees.

Before:

L. Hand, Augustus N. Hand Chase,
Circuit Judges.

Appeal from an order of the District Court for the Southern District of New York, denying a motion to amend a plan of corporate reorganization after confirmation under Chapter X of the Bankruptcy Act. Also two appeals from two other orders, ancillary to the first.

T. Roland Berner, for Knight and Doyle, appellants.

John Gerdes, for Wertheim & Co., et al., appellees.

Louis G. Bernstein, for a committee of other debenture holders, appellees.

Henry S. Hooker, for Duncan, Trustee, appellee.

George T. Barker, for Hudson Maguire, et al., appellees.

George Zolotar, for the Securities and Exchange Commission.

L. Hand, Circuit Judge:

This appeal and two other appeals are from an order and two ancillary orders of the Bankruptcy Court, refusing to submit an "alteration" of a plan of reorganization to the creditors and shareholders of the debtor. The debtor is the owner of a large office building in lower Manhattan, known as the Equitable Office Building, which on April 10, 1941, filed a petition for reorganization under Chapter X. It had but one class of capital stock, which was without par value and consisted of 862,098 shares; it had issued bonds of $16,000,000, secured by a first mortgage; second mortgage bonds, of which only $3000 remained outstanding; and $4,754,000 outstanding of five per cent debentures, due May 1, 1952. The court approved the petition on the day it was filed; but it was not until nearly three years later—on February 24, 1944—that the trustee filed any plan of reorganization under §169. Various amendments were proposed to this from time to time thereafter; but the plan had taken substantially its present form by May 11, 1945.

It provided that the first mortgage of $16,000,000 should remain untouched; that the $3000 remaining due

on the second mortgage should be paid; that a new company should be formed which should issue to the debenture holders convertible income bonds for sixty per cent of their holdings, as well as ten shares of new stock for every $100; that the claims of the unsecured creditors should be paid in full in cash; and that the old shareholders should receive new shares in the ratio of one to ten. The new convertible income bonds were to bear cumulative interest at five per cent, were to mature in thirty-five years and were to be secured by a second mortgage; the bondholders had the right to convert them into new shares, within two years after issue, on the basis of sixteen for each $100; and, within three years after issue, on the basis of ten shares for each $100. The authorized capital of the new company was to be 1,017,933.8 shares, of a par value to be ascertained by the trustee and approved by the court: 475,400 of which would be issued at once to the debenture holders, 456,384 would be reserved against the conversion privilege of the new bonds; and 86,209.8 shares would go to the old shareholders. Administrative and reorganization expenses were to be paid out of the cash in the hands of the trustees. On October 31, 1945, the current liabilities of the debtor were $242,000, together with $950,000 back interest upon the debentures.

Other amendments were proposed by creditors and shareholders after May 11, 1945, but on December 4, 1945, the court approved the plan under § 174 as it had finally taken shape. Notice was then given under § 175 "to all creditors and shareholders who are affected," and the plan came on for confirmation under § 221 on May 13, 1946, when the judge entered an order of confirmation. He signed various auxiliary orders during June and July, which are not important; and on July 8, 1946, entered an order of "consummation." This was not the "final decree" required by § 228, which presupposes earlier "con-

summation"—performance—of the plan; it merely provided in detail the steps necessary to "consummate" the plan. Before the prescribed transfers had been made, two shareholders, Knight and Doyle, on July 11, 1946, filed the petition which is the basis of this appeal, and which proposed, as an "alteration" or "modification" of the plan, an offer, made to the judge and the trustee in a letter of the City Investing Company (a large real estate company). This offer was to give the old shareholders an option to buy the new company's shares at $4.50 a share; to underwrite the issue; to receive as a commission 69,686 shares; and with the money so raised, together with the debtor's liquid assets, to pay off the debentures, principal and interest. The option price was later raised to $5.50, and finally (on July 19th) to $6; the offer was to expire on October 17, 1946.* The judge held extensive hearings at which attorneys representing a substantial number of shareholders appeared and urged the acceptance of the offer; and at which the debenture holders unanimously opposed it, as was readily understandable, since the price of the bonds had risen far above the amount of principal and interest. The court denied the petition in a short memorandum, as follows:

> "The deliberate and fully considered adjudication of a responsible court made and entered without objection on the part of any person in interest—and after all parties were afforded ample opportunity to be heard on the merits of the issues involved—and when they and the public—as they had a right to do—confidently relied upon its integrity, should be something more stable than a weather vane. * * * For

* On November 1, 1946, it would have taken $5,942,500 to pay the debentures with interest; the sale of 862,098 shares at $6 would result in $5,172,588; the deficit of $769,912 would be paid by the cash balance, estimated on November first at $942,500, leaving a cash balance of only about $170,000 as of that date. The estimated income for each month was $315,000, and the estimated operating expenses for the five months of November to March, inclusive, were $104,000 a month.

this reason, my consummation order of July 8, 1946, will stand. It follows that the application to reopen the reorganization proceedings of the debtor will be denied."

It was from this order and two other orders, which it is not necessary here to consider, that Knight and Doyle have appealed.

The appellees argue that the appeal should be dismissed for two reasons: (1) because the bankruptcy judge denied the motions, not for lack of power, but in his discretion; (2) because the offer of the City Investing Company has now long since expired, and the whole controversy has become moot. We agree that the judge did not decide from lack of power, and that he exercised his discretion; indeed, we should have had to assume as much anyway, had not his opinion, just quoted, proved it. Therefore, the order may not be disturbed unless he overstepped the permissible limits of his discretion. We also overrule the other ground for dismissing the appeal: i. e., that it has become moot. It is indeed true that the offer of the City Investing Company has long since lapsed, and that at present there is no outstanding offer; but it does not follow that a new offer may not be made of enough cash to pay off the debentures. That depends upon whether the City Investing Company, or some other company, will make such an offer; we cannot say on this record that the value of the debtor's property has so fallen in the past six months that the equity has for practical purposes disappeared; and indeed the strong resistance of the debenture holders to the appeal suggests that it has not.

The first question on the merits is whether the judge had the power, as he supposed, to submit the offer to the shareholders, because, if, as the appellees insist, he had not, it makes no difference whether he did not keep within

the bounds of a sound discretion. We agree that he did have the power. Chapter X requires that a plan shall first have the "approval" of the judge (§ 174) after the hearing provided in § 169 and § 170. The parties interested must then accept it at a second hearing as provided in § 174, after which it is ready for "confirmation" under § 221. It must then be performed, "consummated" (§§ 224-227), and when "consummated," the judge must enter a "final decree" (§ 228), which discharges the debtor from all its debts, cuts off the shareholders, and discharges the trustee. The Act makes no provisions for any "order of consummation" such as the judge entered on July 8, 1946; and, although it is a convenient way of specifying exactly how the plan is to be performed, as we have already said, it is not to be confused with the "final decree." The order of "confirmation" is not conclusive, for § 222 expressly provides that the plan may be "altered or modified" after, as well as before, the plan has been confirmed. If an "alteration" or a "modification" does not "materially and adversely affect the interests of creditors or stockholders," this may be done without further hearing; otherwise, if it does. It must be observed that, so far as concerns merely the grant of power, the statute makes no difference between the periods before and after confirmation. That does not indeed mean that the fact of confirmation should play no part in the decision whether to use the power; but it does mean that confirmation is only a circumstance in the whole nexus of facts which will determine the question. Against this the debenture holders invoke our decision in **Country Life Apartments v. Buckley,*** and the decision of the Seventh Circuit in **Diversey Building Corp. v. Metropolitan Trust Co.**** In the first, the plan had provided for an outright sale of the property for cash at auction, and the "modification" required the creation of a new

* 145 Fed. (2) 935.

** 141 Fed. (2) 65.

corporation, the shares in which were to be exchanged for claims against the debtor; in the second, the plan had been in operation for nearly eight years after confirmation; under it an old bond issue had been divided into two parts of different priorities; and the "modification" proposed an exchange of one of these new issues for preferred and common shares, and the outright cancellation of the other. We said in our opinion that there was a limit to what might be considered an "alteration" or a "modification" and that the proposal had exceeded it; and the Seventh Circuit spoke of the court's not having "jurisdiction" to act upon the proposal; we agree that, although there appear to be no limits to the changes which may be made in a plan before "approval," and indeed thereafter, until "its submission for acceptance" under § 179, nevertheless any changes after submission must be to some extent congruent with the plan. We cannot, however, agree that there are narrower or more definite limits than this. There is nothing whatever in the joint report of the House and Senate Committee on § 77 B to support such a conclusion. It is true that one clause of that report explained subdivision (f)—the precursor of § 222—as directed to the correction of "errors, mistakes and omissions"; indeed, Congress may have had such modifications in mind as those which would not "adversely affect the interests of creditors or shareholders." But the same clause begins with the words "matters not foreseen," and the proposed "modification" at bar was of that kind: it provided for "matters not foreseen." The plan as confirmed went back at least to December, 1945, and more properly to May, 1945, and the rise in value of the Debtor's property which prompted the offer of the City Investing Company could not have been then foreseen. Nor were the proposed changes themselves so radical as to fall within our decision in **Country Life Apartments v. Buckley**, supra.* The first mortgage was

* 145 Fed. (2) 935.

to remain as before; the balance upon the second mortgage was to be paid as before; a new corporation was to be organized with the same capital as before; the old shareholders were to have the same number of new shares as before; the current liabilities were to be paid as before. The only change was that the debenture bonds were to be paid in cash instead of refunded in new bonds and new shares, and that to do this the shares which had been reserved for them, either immediately, or to answer their conversion privilege, were to be sold to the old shareholders, taken up by the City Investing Company, or were to go to that company for its underwriting commission.

There remains the question whether the judge, having power to accept the "alteration," was free as matter of discretion to reject it. The only considerations which, so far as we can see, might properly have moved him to do so were (1) a conflict of interest between the debenture holders and the shareholders; (2) the fact that after long years of delay the reorganization had finally culminated in a confirmed plan, and (3) doubts that the new company would be too much stripped of liquid assets to keep afloat. These we shall take up seriatim. We cannot agree that the debenture holders had as yet any legally protected interest in the property beyond the principal and accrued interest of their bonds, which could be weighed against the shareholders' interest. If in fact they had relied upon sharing in an equity in the property above that amount, it was without warrant of law and constituted no reason for depriving the shareholders of whatever chance might remain of realizing upon their property. The debenture holders were in truth not "adversely affected" by the proposed "alteration," within the meaning of § 222. It is, of course, true that there must come a time when a mortgagee or a creditor, who takes over his debtor's property in extinguishment of the debt, gets an indefeasible title, just as the

mortgagee did in equity upon final decree of strict foreclosure; but Chapter X provides its own date when this shall occur; it is the date of the entry of the "final decree" under § 228. It is that decree which puts an end to "all rights and interests of stockholders" and discharges all "debts and liabilities" of the debtor. Until then creditors remain creditors; they have their claims and that is all they have; any "modification" which guarantees them principal and interest on those claims, secures all the rights that a court need regard. The offer of the City Investing Company of July 11, 1946, did that; and we answer the first question that there was no party to the reorganization whose interest the judge could properly weigh against that of the shareholders, except in so far as by further delay the debenture holders' claims might be imperiled.

Next as to that delay and as to the fact that the plan had been confirmed. We recognize that, except upon the extremest provocation, courts will not upset a judicial sale at auction, upon the ground that a new bidder has appeared who offers more than the knock-down price. **Morrison v. Burnette,*** **In re Burr Manufacturing and Supply Co.,**** **Currin v. Nourse.***** This unwillingness results from the effect upon such sales of knowing that a prospective bidder may abstain from bidding at the auction, may bide his time, and may then outbid the price at which the property has been struck down. That possibility tends to chill bidding at the sale, to dispose of the property by later competition on successive bids, and thus to defeat the very purpose of an auction, which is to fetch together all those who may be interested to buy and to set them against each other with whatever stimulus that may provide, as opposed to other kinds of sale. None of this applies to a plan of reorganiza-

* 154 Fed. Rep. 617, 624 (C. C. A. 8).

** 217 Fed. Rep. 16 (C. C. A. 2).

*** 66 Fed. (2) 137, 140 (C. C. A. 8).

tion. True, that presupposes a concourse of conflicting interests—creditors of different priorities and shareholders of different ranks—whose compromise in the plan itself will be a result of competition. But there is no occasion when all are brought together and pitted against each other in a cash bidding, i. e., there is no occasion equivalent to an auction whose finality must be preserved if its advantages are to be preserved.

That does not indeed mean that delay in presenting an "alteration" or "modification" can never be relevant to its approval; we recognize the force of what the judge said in his opinion, which we have quoted, that the considered judgment of a court is not to be lightly put aside. But there can be considerations more imperative than the despatch of judicial business, even after delays so long as existed in this case. If the legally protected interests of any opposing parties are fully preserved, it is not a good reason to deny others any reasonable chance to protect their own interests that they have been long in asserting them. Had it been shown that the equity which was presupposed in the proposal of the City Investing Company had existed for a substantial time before July 11, 1946, there would be force in what the judge said in his opinion; but that was not shown; so far as appears, the equity may have arisen from a recent increase in the value of the property. Delay would not cost the debenture holders anything, for the proposal would give them interest until payment upon the full face of their bonds instead of upon sixty per cent of it; and the property was adequate security.

The last question remains, whether the new company would have been so stripped of quick assets that it might prove unable to carry on its business, i. e., that its cash resources would have been at the danger point. This must be judged on the assumption that the debenture bonds

would be paid off, and that the new company would owe nothing but its first mortgage bonds. There would be a little over a million shares of common stock behind the mortgage, of which the old shareholders would hold 86,000, the City Investing Company about 70,000 and the remainder would be distributed between the two, according as the shareholders should have taken up their options. The amount of cash which would be left to carry on was necessarily speculative; but the prospect was undoubtedly of a much smaller margin than had been the company's habit in the past; perhaps it was so small that a majority of the shareholders would have preferred to take ten per cent of their holdings and let the option go. That was, however, not a question for the debenture holders or for the trustee; indeed, it was not even a question for the judge. It was for a majority of the shareholders, and for them alone, to decide whether they preferred to accept the chance of being able to pay the interest on the first mortgage; and if they chose to do so, the judge would not have been justified in interfering in their choice; it was a practical decision within the powers of the majority; Chapter X does not give to the bankruptcy court any larger supervision in such a situation than if the new company had been set up and sent upon its way.

In conclusion, therefore, we can see no reason why the "alteration" should not have been submitted under § 222; and we hold that it was an error to deny the petition. Upon remand the question will be whether the City Investing Company—or for that matter, any other equally responsible underwriter—will within a reasonable time come forward with a reliable and practical offer which will produce enough money to pay off the debenture bonds, principal and interest. If such an offer is forthcoming, it should be treated as a permissible "alteration" or "modification" of the plan under § 222, and the judge should "approve" it,

provided he finds that it satisfies the conditions we have just mentioned. Thereupon he should fix a hearing for its "consideration" under § 222, and "a subsequent time for its acceptance or rejection" under §§ 222 and 223. Since the only persons whose interest can be "adversely affected" by such a change in the plan, are the shareholders, it follows that their votes alone will determine acceptance or rejection. Section 222 speaks in the alternative: creditors "or" shareholders. It is not necessary to say anything of the two ancillary orders; they necessarily fall with the main order.

Orders reversed.

APPENDIX E.

Bankruptcy Act, Section 77 (e).

[U. S. C., 205 (e).]

Court Hearing After Approval by Commission; Acceptance of Plan by Creditors and Stockholders; Confirmation of Plan by Court; Valuation of Property.

(e) Upon the certification of a plan by the Commission to the court, the court shall give due notice to all parties in interest of the time within which such parties may file with the court their objections to such plan, and such parties shall file, within such time as may be fixed in said notice, detailed and specific objections in writing to the plan and their claims for equitable treatment. The judge shall, after notice in such manner as he may determine to the debtor, its trustee or trustees, stockholders, creditors, and the Commission, hear all parties in interest in support of, and in opposition to, such objections to the plan and such claims for equitable treatment. After such hearing, and without any hearing if no objections are filed, the judge shall approve the plan if satisfied that: (1) it complies with the provisions of subsection (b) of this section, is fair and equitable, affords due recognition to the rights of each class of creditors and stockholders, does not discriminate unfairly in favor of any class of creditors or stockholders, and will conform to the requirements of the law of the land regarding the participation of the various classes of creditors and stockholders; (2) the approximate amounts to be paid by the debtor, or by any corporation or corporations acquiring the debtor's assets, for expenses and fees incident to the reorganization, have been fully disclosed so far as they can be ascertained at the date of such hearing, are reasonable, are within such maximum limits as are fixed by the Commission, and are within

such maximum limits to be subject to the approval of the judge; (3) the plan provides for the payment of all costs of administration and all other allowances made or to be made by the judge, except that allowances provided for in subsection (c), paragraph (12) of this section, may be paid in securities provided for in the plan if those entitled thereto will accept such payment, and the judge is hereby given power to approve the same.

If the judge shall not approve the plan, he shall file an opinion, stating his conclusions and the reason therefor, and he shall enter an order in which he may either dismiss the proceedings, or in his discretion and on motion of any party in interest refer the proceedings back to the Commission for further action, in which event he shall transmit to the Commission a copy of any evidence received. If the proceedings are referred back to the Commission, it shall proceed to a reconsideration of the proceedings under the provisions of subsection (d) of this section. If the judge shall approve the plan, he shall file an opinion, stating his conclusions and the reasons therefor, and enter an order to that effect, and shall send a certified copy of such opinion and order to the Commission. The plan shall then be submitted by the Commission to the creditors of each class whose claims have been filed and allowed in accordance with the requirements of subsection (c) of this section, and to the stockholders of each class, and/or to the committees or other representatives thereof, for acceptance or rejection, within such time as the Commission shall specify, together with the report or reports of the Commission thereon or such a summarization thereof as the Commission may approve, and the opinion and order of the judge: Provided, That submission to any class of stockholders shall not be necessary if the Commission shall have found, and the judge shall have affirmed the finding, (a) that at the time of the finding the corporation is insolvent, or that at the time of the finding the

equity of such class of stockholders has no value, or that the plan provides for the payment in cash to such class of stockholders of an amount not less than the value of their equity, if any, or (b) that the interests of such class of stockholders will not be adversely and materially affected by the plan, or (c) that the debtor has pursuant to authorized corporate action accepted the plan and its stockholders are bound by such acceptance: Provided further, That submission to any class of creditors shall not be necessary if the Commission shall have found, and the judge shall have affirmed the finding, that the interests of such class of creditors will not be adversely and materially affected by the plan, or that at the time of the finding the interests of such class of creditors have no value, or that the plan provides for the payment in cash to such class of creditors of an amount not less than the value of their interests. For the purpose of this section the acceptance or rejection by any creditor or stockholder shall be in writing, executed by him or by his duly authorized attorney, committee, or representative. If the United States of America, or any agency thereof, or any corporation (other than the Reconstruction Finance Corporation) the majority of the stock of which is owned by the United States of America, is a creditor or stockholder, the interests or claims thereof shall be deemed to be affected by the plan, and the President of the United States, or any officer or agency he may designate, is hereby authorized to act in respect of the interests or claims of the United States or of such agency or other corporation. The expense of such submission shall be certified by the Commission and shall be borne by the debtor's estate. The Commission shall certify to the judge the results of such submission.

Upon receipt of such certification, the judge shall confirm the plan if satisfied that it has been accepted by or on behalf of creditors of each class to which submission

is required under this subsection holding more than two-thirds in amount of the total of the allowed claims of such class which have been reported in said submission as voting on said plan, and by or on behalf of stockholders of each class to which submission is required under this subsection holding more than two-thirds of the stock of such class which has been reported in said submission as voting on said plan; and that such acceptances have not been made or procured by any means forbidden by law: Provided, That, if the plan has not been so accepted by the creditors and stockholders, the judge may nevertheless confirm the plan if he is satisfied and finds, after hearing, that it makes adequate provision for fair and equitable treatment for the interests or claims of those rejecting it; that such rejection is not reasonably justified in the light of the respective rights and interests of those rejecting it and all the relevant facts; and that the plan conforms to the requirements of clauses (1) to (3), inclusive, of the first paragraph of this subsection (e); Provided further, That if, in any reorganization proceeding under this section, the United States is a creditor on claims for taxes or customs duties (whether or not the United States has any other interest in, or claim against, the debtor, as creditor or stockholder), no plan which does not provide for the payment thereof shall be confirmed by the judge except upon the acceptance, certified to the court, of a lesser amount by the President of the United States or the officer or agency designated by him pursuant to the provisions of the preceding paragraph hereof: Provided further, That if the President of the United States or such officer or agency shall fail to accept or reject such lesser amount for more than ninety days after receipt of written notice so to do from the court, accompanied by a certified copy of the plan, the consent of the United States insofar as its claims for taxes or customs duties are concerned shall be conclusively presumed. If the judge shall confirm the

plan, he shall enter an order and file an opinion with a statement of his conclusions and his reasons therefor. If the judge shall not confirm the plan, he shall file an opinion, with a statement of his conclusions and his reasons therefor, and enter an order in which he shall either dismiss the proceedings, or, in his discretion and on the motion of any party in interest, refer the case back to the Commission for further proceedings, including the consideration of modifications of the plan or the proposal of new plans. In the event of such a reference back to the Commission, the proceedings with respect to any modified or new plan shall be governed by the provisions of this section in like manner as in an original proceeding hereunder.

If it shall be necessary to determine the value of any property for any purpose under this section, the Commission shall determine such value and certify the same to the court in its report on the plan. The value of any property used in railroad operation shall be determined on a basis which will give due consideration to the earning power of the property, past, present, and prospective, and all other relevant facts. In determining such value only such effect shall be given to the present cost of reproduction new and less depreciation and original cost of the property, and the actual investment therein, as may be required under the law of the land, in light of its earning power and all other relevant facts.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1946

Nos. 879, 909 & 936

No. 879

SOUTHERN PACIFIC COMPANY,
a railroad corporation, Intervener,
Petitioner,

v.

BERRYMAN HENWOOD, as Trustee of St. Louis Southwestern Railway Company Lines, *et al.*,
Respondents.

No. 909

WALTER E. MEYER, Intervener,
Petitioner,

v.

BERRYMAN HENWOOD, as Trustee of St. Louis Southwestern Railway Company Lines, *et al.*,
Respondents.

No. 936

ST. LOUIS SOUTHWESTERN RAILWAY COMPANY,
a Corporation, Debtor,
Petitioner,

v.

BERRYMAN HENWOOD, as Trustee of St. Louis Southwestern Railway Company Lines, *et al.*,
Respondents.

BRIEF OF PROTECTIVE COMMITTEE FOR HOLDERS OF ST. LOUIS SOUTHWESTERN RAILWAY COMPANY FIRST TERMINAL AND UNIFYING MORTGAGE BONDS, INTERVENER, IN OPPOSITION TO PETITIONS FOR WRITS OF CERTIORARI.

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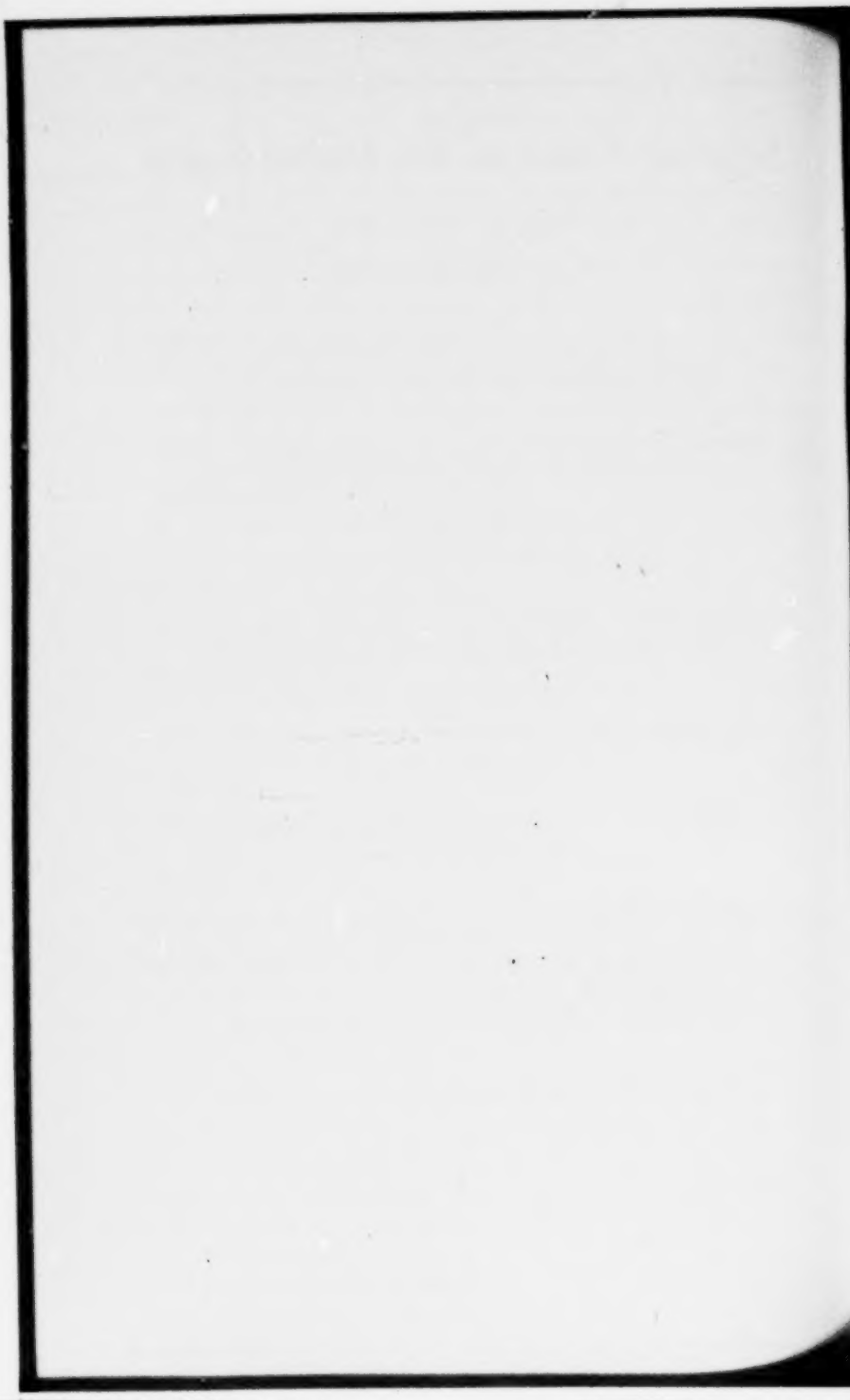

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1946

Nos. 879, 909 AND 936

No. 879

SOUTHERN PACIFIC COMPANY,
a railroad corporation, Intervener,
Petitioner,

v.

BERRYMAN HENWOOD, as Trustee of St. Louis Southwestern Railway Company Lines, *et al.*,
Respondents.

No. 909

WALTER E. MEYER, Intervener,
Petitioner,

v.

BERRYMAN HENWOOD, as Trustee of St. Louis Southwestern Railway Company Lines, *et al.*,
Respondents.

No. 936

ST. LOUIS SOUTHWESTERN RAILWAY COMPANY,
a Corporation, Debtor,
Petitioner,

v.

BERRYMAN HENWOOD, as Trustee of St. Louis Southwestern Railway Company Lines, *et al.*,
Respondents.

BRIEF OF PROTECTIVE COMMITTEE FOR HOLDERS OF ST. LOUIS SOUTHWESTERN RAILWAY COMPANY FIRST TERMINAL AND UNIFYING MORTGAGE BONDS, INTERVENER, IN OPPOSITION TO PETITIONS FOR WRITS OF CERTIORARI.

OPINIONS BELOW.

The opinion of the Circuit Court of Appeals herein (R. 5559-5680) is reported at 157 F. (2d) 337. The opinion of

the District Court (R. 5183-5212) is reported at 53 F. Supp. 914. The initial Report of the Interstate Commerce Commission (R. 3495-3735) is reported at 249 I. C. C. 5, and its Supplemental Report (R. 3736-3820) at 252 I. C. C. 325.

STATUTES INVOLVED.

Because of their length, Sections 77(d), (e) and (g) of the Bankruptcy Act (11 U. S. C. sec. 205(d), (e) and (g)) are printed as Appendix A to this brief.

SUMMARY OF ARGUMENT.

I. The contentions of Walter E. Meyer contained in Points I, II and III of his brief, were fully considered and properly decided by the Interstate Commerce Commission, by the District Court and by the Circuit Court of Appeals, and there is, therefore, no reason for this Court to exercise its discretion to review.

II. It was within the discretion of Judge Moore to deny the motion of Walter E. Meyer for new hearings, and such discretion was properly exercised.

III. The question *vel non* the debtor is now solvent, is irrelevant and immaterial in this reorganization.

IV. The so-called "changed conditions" were in the contemplation of the Interstate Commerce Commission at the time it formulated the plan of reorganization.

ARGUMENT.

POINT I.

The contentions of Walter E. Meyer contained in Points I, II and III of his brief, were fully considered and properly decided by the Interstate Commerce Commission, by the District Court and by the Circuit Court of Appeals, and there is, therefore, no reason for this Court to exercise its discretion to review.

In *Group of Institutional Investors v. Chicago, Milwaukee, St. Paul & Pacific Railroad Co.*, (1943) 318 U. S. 523, 545, this Court said:

> "Elimination of delay in railroad receivership and foreclosure proceedings was one of the purposes of the enactment of §77. Continental Illinois National Bank & Trust Co. v. Chicago, Rock Island and Pacific R. Co., 294 U. S. 648, 685. Section 77(g) giving the District Court power to dismiss the proceedings for 'undue delay in a reasonably expeditious reorganization' was inserted in recognition of 'the necessity of prompt action'. (H. Rep. No. 1283, 74th Cong. 1st Sess. p. 3) We cannot conclude that in this proceeding which already has been pending seven years and which was before the Commission for over four years, the interests of junior claimants have been sacrificed for speed."

These proceedings were first instituted on December 12, 1935 (R. 24-32). Sixteen months later, by April 24, 1937, all plans of reorganization had been filed and hearings completed before the Interstate Commerce Commission (R. 3497). This initial expedition ended with those hearings when the delaying activities of Mr. Meyer started. Those activities were succinctly set forth on pages 9 to 16 inclusive of the "Brief of Southern Pacific Company, in Reply to Brief of Appellant Walter E. Meyer, in Reply to Motion for Stay or Remand by Appellant Walter E. Meyer,

and in Respect of Amicus Brief of the United States" dated March 19, 1945, and filed with the United States Circuit Court of Appeals for the Eighth Circuit. Rather than paraphrase that concise historical statement, it is quoted here in full:

> "As to the proceedings before the Commission: On December 7, 1936, within the time allowed therefor, the Debtor filed a plan of reorganization with the Commission, and other plans were filed by other parties (R. 3496). Hearings upon the plan of reorganization were held on March 16, 1937, were recessed, and were concluded on April 24, 1937 (R. 3497). At these hearings, the Appellant Meyer presented various contentions and charges against Southern Pacific Company, which were summarized and disallowed in the proposed report of Examiner J. V. Walsh, filed February 7, 1938 (R. 255, 306-314). The case was argued upon exceptions to the proposed report on May 16, 1938 (R. 3496). A petition was filed in April, 1937, by Appellant Meyer for an investigation by the Commission and for such other relief as might seem meet in respect of his charges against Southern Pacific Company and others (R. 339 to 351). This was amplified by a supplemental petition filed in June, 1937 (R. 357 to 467), in which the prayer requested, in addition to an investigation, an opportunity for the petitioner to introduce evidence at reopened hearings. The Commission on January 25, (*sic*) 1939, entered an order reciting the petition by Appellant Meyer and directing that the proceeding be reopened, 'with respect to the matters alleged in said petitions, in so far as they may be relevant and material in this proceeding' (R. 501). A hearing pursuant to this order was held from May 5, 1939, to May 27, 1939, and from September 18, 1939, to September 30, 1939 (R. 3549). At these hearings, Meyer presented his case relative to his charges against Southern Pacific Company and others, and his adversaries presented testimony on their part. The hearings were conducted by Commissioner Clyde B. Aitchi-

son and Examiner Walsh. On June 30, 1941, the Commission issued its report, one Commissioner dissenting on this phase, in which it generally and specifically found against each and every contention of the Appellant Meyer (R. 3547 to 3678). A petition for modification was filed by the Appellant Meyer, along with petitions by others for modification of other phases of the report, and the Commission on March 9, 1942, issued its supplemental report maintaining and elaborating upon its findings against Meyer's contentions (R. 3742 to 3752).

"As to the proceedings in the Court below: We have referred to the pleas by Appellant Meyer and others in opposition to the petition for reorganization and the findings of December 31, 1935, made by the Honorable Charles B. Davis sitting in the Court below, overruling his contentions (R. 87 to 93). In accordance with Title 11, U. S. C. A., §205(c)(7), directing that the judge shall promptly determine and fix the time within which claims may be filed and the manner in which they may be evidenced and allowed, the Court by its Order No. 28, dated February 5, 1936 (R. 3953 to 3955), and by its Order No. 81, dated May 22, 1936 (R. 3955 to 3961), fixed times and procedures in respect of the filing of claims. By its Order No. 184, dated April 13, 1937, it provided an extended time for the filing of protests and objections to allowances of any claims which had been filed. This Order read (R. 3962):

> "'1. That the time within which parties in interest may file protests or objections to the allowance of any claims for which proofs of claim have been filed herein, be and it hereby is extended (a) as to proofs of claim of mortgage trustees or others filed under the provisions of Order No. 81, to and including May 15, 1937, and (b) as to all other proofs of claim, to and including July 15, 1937.'

By its Order No. 272, dated February 25, 1938 (R. 3962 to 3965), it referred the determination of claims to the Honorable Marion C. Early, Special Master. Pursuant

to these orders, the Reconstruction Finance Corporation, on March 18, 1936, filed its claim in respect of the indebtedness of the St. Louis Southwestern Railway Company to it on account of note for the principal sum of $17,882,250 and for interest thereon (R. 3965 to 3975). Upon the payment by the Southern Pacific Company of this note, guaranteed as to collection by it, the Reconstruction Finance Corporation assigned the note and claim to Southern Pacific Company, which assignment was filed with the Court July 21, 1936 (R. 3975 to 3981). Within the time allowed therefor, two corporations, Anglo-Continentale Treuhand, A. G., and Mondiale Handels-und Verwaltungs, A. G., filed protests to the assigned claim held by Southern Pacific Company (R. 3982 to 3984). After extended hearings, the Master, Marion C. Early, filed with the Court on August 25, 1939, his findings of fact and conclusions of law (R. 3985 to 3995). His findings include the following (R. 3991):

> " 'The St. Louis Southwestern Railway Company was operated as a separate and distinct corporation, and its accounts and affairs were not commingled in any way with those of Southern Pacific Company, and its officers, including that of President, devoted their entire time to its affairs, while Messrs. Holden and McDonald, who also held positions with Southern Pacific Company, devoted only a portion of their time to the affairs of the St. Louis Southwestern Railway Company. Southern Pacific Company made no loans or advancements to St. Louis Southwestern Railway Company, but its Board of Directors adopted a resolution in January, 1935, to advance it loans on open account not to exceed in the aggregate $100,000.00. No advancements or loans were made, however, under authority of this resolution.
>
> " 'Claimant, the Southern Pacific Company, and St. Louis Southwestern Railway Company were at all times conducted as independent corporations, kept separate books, and the funds of the

two companies were never commingled, and I find that Claimant did not overreach, coerce or take any advantage of Debtor, St. Louis Southwestern Railway Company, by reason of the fact that it owned approximately 87 per cent of its capital stock.'

The Master recommended that the claim be allowed (R. 3994). Exceptions were taken to the report of the Special Master by the protestant corporations (R. 3996), and the Court, upon submission of the matter to it, on January 26, 1940, held that the report of the Special Master should be sustained, the protests disallowed, and the claim of Southern Pacific Company allowed (R. 4002, 4003). No appeal was taken to this Court from this order by any party to these proceedings. On March 23, 1942, the Commission, as provided by Title 11, U. S. C. A., §205(e), certified the plan of reorganization, as modified by its supplemental report, to the Court below (R. 3494). On May 29, 1942, appellant Walter E. Meyer, among others, filed objections in the Court to the plan of reorganization (R. 3840). These objections contained various charges against the Southern Pacific Company and requested, among other things, that the interest of Southern Pacific Company as a creditor and stockholder be expunged or at least subordinated to all other creditors and stockholders of the Debtor (R. 3842). On June 9, 1942, Meyer was permitted to intervene as a party to the proceedings in the Court below (R. 4006). After the overruling on July 13, 1942, of a motion by the appellant Meyer to take further testimony and obtain further documentary evidence, for the reason that his motion tended to unduly enlarge the subject matter of the inquiry and was calculated to retard and prolong the consideration of the plan of reorganization (R. 4007), the plan of reorganization and the various objections thereto came on for hearing on October 26, 1942 (R. 4051). A great deal of testimony was introduced, principally by the appellant Meyer. The hearing, which

was before Judge Davis, was concluded on November 5, 1942 (R. 4993), with provision for additional arguments to be made at a later date for appellant Meyer and the Debtor, and for the filing of briefs by all the parties. Subsequently, before these arguments were made and briefs filed, Judge Davis died, and Judge Moore called the parties for a conference on April 23, 1943, to ascertain their views as to further procedure (R. 5137). All the parties interested except Meyer urged Judge Moore to consider the case upon the record as certified to the Court by the Commission and upon the evidence as taken by Judge Davis. Appellant Meyer took the position that there should be a new trial before Judge Moore (R. 5170, 5179), although he did not object to the Court considering the testimony which had been taken, provided that he could introduce new testimony (R. 5170, 5180). After the conference the Court entered an order (R. 5181-5183) taking the case as submitted on the record as made before the Commission and on the testimony as taken before Judge Davis, with provision for oral argument on May 31, 1943, and for briefs. There was a provision in the order that the Court would entertain any motion of any party for the taking of additional testimony or otherwise pertaining to the completion of the record (R. 5182). In accordance with this order, all of the parties so desiring argued the case before Judge Moore and filed briefs. Appellant Meyer argued orally and filed briefs with Judge Moore but filed no motion for the taking of additional testimony or otherwise as to the completion of the record. On February 9, 1944, Judge Moore rendered his opinion and order approving the plan of reorganization and overruling all of the objections thereto, including those of the appellant Meyer (R. 5183 to 5213). On March 9, 1944, Meyer filed his notice of appeal to this Court from this judgment (R. 4).

"This Court should also have before it an outline of the Appellant Meyer's connection with the Debtor.

"Mr. Meyer, a member of the Bar of the State of New York since 1903 (R. 1350), made an investment in St. Louis Southwestern Railway Company stock as early as 1920 (R. 530). Thereafter he dealt heavily and extensively in St. Louis Southwestern Railway Company stock, buying and selling, but on the balance being a purchaser (Meyer's Exhibit No. 262 before the Commission, R. 1049), so that his total investment became $964,319.20 (R. 531). He was also an active investor in other properties and had other business interests (R. 1350 to 1351). However, a large share of his time was given over to the St. Louis Southwestern (R. 1351). He intervened as a party, in opposition to the management of the St. Louis Southwestern Railway Company, in many proceedings before the Commission (R. 533). He continuously objected to the conduct of the Railway Company's affairs by the management and circularized at times the stockholders of the St. Louis Southwestern Railway Company. These activities were initiated as early as 1925 and long before the Southern Pacific Company had any relationship with the St. Louis Southwestern Railway Company, other than as a connecting carrier. Examples of these activities, prior to Southern Pacific Company acquisition of stock of the St. Louis Southwestern Railway Company, appear in the record (R. 539, 540, 577, 689). There also appear in the record examples of the observations of prior managements of the St. Louis Southwestern concerning Meyer (R. 699, 712, 716). After Southern Pacific Company acquired the stock of the St. Louis Southwestern Railway Company, these activities continued, but were directed at Southern Pacific Company. Charges against it were circularized among St. Louis Southwestern security holders (R. 835, 838). Not content with this, attacks on Southern Pacific officers who had displeased him, were distributed by Meyer among Southern Pacific stockholders (R. 1032, 1042). These were appropriately answered (R. 1040). The Commission quoted the views of the Debtor's officers of Meyer's conduct in its report (R.

3612, 3613) and reaffirmed its findings in its supplemental report, despite his request that they be stricken (R. 3752). While Meyer was making and publicizing his attacks upon the St. Louis Southwestern management, he was increasing his stockholdings by purchases in the market (R. 634, 1467-1469; *Cf.* R. 1049). Many railroads in the Western territory, national banking houses, and others, were brought within the range of the appellant's attacks. Some ninety-odd persons were defendants in a stockholder's derivative action brought by Walter E. Meyer to recover $30,000,000 in 1934 (R. 1011). The suit was dismissed upon jurisdictional grounds, *Meyer, et al.* v. *Kansas City Southern, et al.*, 11 F. Supp. 937, affirmed (C. C. A. 2d) 84 F. (2d) 411, certiorari denied 299 U. S. 607. Claims of persecution were made against Mr. Henry W. de Forest, a Southern Pacific Company director and officer, although the appellant's contact with him had been slight (R. 1405 to 1415). Of this the Commission says (R. 3566):

> "'Meyer, in support of his charge that the filing of the petition for reorganization was directed by de Forest as an act of resentment and with a fixed determination to destroy the debtor, points to no suggested basis therefor except de Forest's advanced age, and except that he suggests that he may have been instrumental in forcing de Forest's resignation as chairman of the Southern Pacific Company. Testifying at the hearing, April 24, 1937, [R. 173 to 216] in response to Meyer's subpoena, de Forest gave no indication of any resentment or malice toward Meyer; and stated that his resignation was voluntary, and due to his age. At the time of the further hearing, de Forest was deceased. The charge is without foundation, so far as the record shows.'

With the passage of time, the range of attack expanded. Several years ago it came to include the Illinois Central Railroad Company and the Union Pacific Railroad Company which were alleged to dominate the South-

ern Pacific Company, upon grounds tenuous and fantastic (R. 3021 to 3038, 4832 to 4865). Although such charges do not merit serious consideration, it may be noted that the Commission with its usual meticulousness found them unfounded (R. 3551). The Trustee of the Debtor, Berryman Henwood, appointed by the Honorable Charles B. Davis in the Court below, in accordance with the direction of the Court (R. 3902) and the mandate of the statute, Title 11, U. S. C. A., §205(c)(9), rendered reports as to whether or not there were irregularities, fraud, misconduct or mismanagement of the Debtor's affairs. These reports are in the record (R. 3903 to 3951). Because the Trustee did not find as a result of his investigations any facts indicating to him the existence of irregularities, fraud, misconduct or mismanagement, e.g., R. 3950, Appellant Meyer accuses the Trustee of submitting to Southern Pacific Company control (p. 217, his brief), and of being perfunctory in the performance of his duties (R. 1664, 1665) (p. 271, his brief). The Appellant Meyer's brief herein dated February 14, 1945, his motion that appeal be stayed or proceedings remanded dated November 18, 1944, and his accusations directed against parties and counsel in the oral hearings heretofore held in Court, are further developments. The Commission, which had extensive opportunity to observe and study the Appellant Meyer in the hearings before it, made its findings in its report as to the purpose or motive for these activities, as follows (R. 3674):

> " 'Meyer had been made an offer for his stock in the debtor, which we had found sufficient in the Control case, *supra;* and his apparent animating purpose has been to obtain from the Southern Pacific a consideration for his stock in excess of that offer.'

This finding it reaffirmed in its supplemental report (R. 3752)."

Further evidence of the full opportunity afforded Mr. Meyer to present his contentions, and of the full consideration given thereto by the Interstate Commerce Commission, by the District Court and by the Circuit Court of Appeals, is found in their reports and opinions. In the initial report of the Interstate Commerce Commission (*St. Louis Southwestern Ry. Co. Reorganization*, 249 I. C. C. 5, R. 3495-3713), out of the total of 219 pages, 131 pages (R. 3547-3678), or almost 60 per centum of the entire report was devoted to a detailed analysis and consideration of Mr. Meyer's charges. Further, Commissioner Eastman wrote a dissenting report of 19 pages (R. 3713-3732) devoted wholly to Mr. Meyer, but the Commissioner's dissent was based on a desire to reopen the hearings to explore the suggested unification of the Debtor with Southern Pacific Railroad Company (R. 3731-3732) and not on Mr. Meyer's charges. In his dissent he characterized Mr. Meyer's activities in this sentence (R. 3724):

> "Brooding over this succession of events, I think that Meyer has conjured up conspiracies which go beyond the reasonable probabilities of the situation."

In the opinion of the District Court (R. 5183-5212), of the 29 pages of the opinion, 7 (R. 5197-5203) were devoted to Mr. Meyer's claims, or 24 per centum of the total. In the opinion of the Circuit Court of Appeals (R. 5563-5680), 83 pages (R. 5569-5652) out of the total of 117 pages of text, contain detailed consideration of Mr. Meyer's charges, or 70 per centum of the entire opinion.

It thus appears that Mr. Meyer's contentions have been fully presented to and considered by the various tribunals to which he has submitted them. Mr. Meyer, in his Petition for Writ of Certiorari and supporting brief has failed to show any special and important reason to justify this

Court in exercising its discretion to grant the writ. Since this proceeding has been pending more than twelve years and was before the Interstate Commerce Commission for over five years, it does not seem that the interests of the stockholders have been sacrificed by any failure to consider any and all matters presented.

POINT II.

It was within the discretion of Judge Moore to deny the motion of Walter E. Meyer for new hearings, and such discretion was properly exercised.

In substance, what Mr. Meyer sought was an opportunity again to present his case before a new judge, or a new trial. That a successor judge has the power to pass upon a motion for a new trial, has long been upheld in this Court. In *Re The Life and Fire Insurance Company of New York v. The Heirs of Wilson*, 8 Pet. 291, 303 (1833), this Court said:

> "In this case, the district judge seems to think that as the judgment was not rendered by him, he has no power to grant a new trial, as he is not acquainted with the facts and circumstances which should influence his discretion in making such an order; and that, consequently, he is not bound to sanction the judgment by his signature. * * *
>
> "But the district judge is mistaken in supposing that no one but the judge who renders the judgment can grant a new trial. He, as the successor of his predecessor, can exercise the same powers, and has a right to act on every case that remains undecided upon the docket, as fully as his predecessor could have done. The court remains the same, and the change of the incumbents cannot and ought not, in any respect, to injure the rights of litigant parties."

It seems clear, therefore, that Judge Moore had the power to pass upon, and therefore, to refuse, Mr. Meyer's motion for a new trial.

In that event, it is necessary to examine into the question of whether Judge Moore abused his discretion in so exercising that power. The Bankruptcy Act provides (11 U. S. C. §205(d)):

> "The Commission, if it approves a plan, shall thereupon certify the plan to the court together with a transcript of the proceedings before it and a copy of the report and order approving the plan."

The only statutory reference to additional evidence before the court is an indirect one in subdivision (e), (11 U. S. C. §205(e)):

> "If the judge shall not approve the plan, he shall file an opinion, stating his conclusions and the reason therefor, and he shall enter an order in which he may either dismiss the proceedings, or in his discretion and on motion of any party in interest refer the proceedings back to the Commission for further action, in which event he shall transmit to the Commission a copy of any evidence received."

In *Ecker v. Western Pacific Railroad Corporation*, 318 U. S. 448 (1943), this Court clearly set forth its views that the determination of the plan was, in the first instance, for the Commission, and that the court had only a limited review. This was reaffirmed in *Group of Institutional Investors v. Chicago, Milwaukee, St. Paul & Pacific Railroad Company*, 318 U. S. 523 (1943) and in *Reconstruction Finance Corporation v. Denver & Rio Grande Western Railroad Company*, ... U. S. ..... (June 10, 1946) (90 L. ed. 1134).

It thus appears that under the statute, as interpreted and applied by this Court, the District Court is to act upon the record before the Interstate Commerce Commission. The District Court, however, in its discretion, may receive addi-

tional evidence. In the *Western Pacific* Case, this Court said (1. c. 477):

> "Thus, while judicial review does not involve an independent examination into valuation, it does require that the court shall be satisfied, upon the record before the Commission, with such additional evidence as may be pertinent to the objections to the Commission's finding of value, that the statutory requirements have been followed."

And in the *Milwaukee* Case (1. c. 542):

> "As we have indicated in the Western Pacific Railroad Corporation Case, the power of the District Court to receive additional evidence may aid it in determining whether changed circumstances require that the plan be referred back to the Commission for reconsideration."

To recapitulate, the District Court is to pass upon the plan upon the record before the Interstate Commerce Commission with such additional evidence, if any, as the court may see fit to receive. Therefore, as to the record before the Commission, Judge Moore was in the same position as Judge Davis. The only ground for error, therefore, would be Judge Moore's action in considering the record made before Judge Davis.

It would appear to be patently absurd to further delay this reorganization where a part of the record was made before an administrative body and a part before another judge of the same court, because such latter part was not made before the judge who acted. This absurdity is emphasized by the further facts that undoubtedly the judge could have had the testimony taken before a master, that the Judge who acted heard arguments by all interested parties, and that he expressed himself as willing to receive motions "respecting the taking of additional testimony or otherwise pertaining to the completion of the record on

said Plan" (R. 5182), but no one, not even Mr. Meyer, made any such motion.

If Judge Moore had disregarded the testimony introduced before Judge Davis, Judge Moore would have complied strictly with the statute, and since no motion had been made to him respecting additional testimony, he could not be said to have abused his discretion by refusing to receive further testimony. Nor can he be held to have abused his discretion by acting on one transcript (from the Interstate Commerce Commission) and refusing to reject another (before Judge Davis), particularly when the witnesses in the different hearings were substantially the same, and most of the evidence before Judge Davis was documentary.

Point III.

The question vel non the debtor is now solvent, is irrelevant and immaterial in this reorganization.

The three petitioners before this Court urge that subsequent to the Supplemental Report of the Interstate Commerce Commission (R. 3736), the assets of the debtor exceed its liabilities, i. e., that the debtor is "solvent" in the bankruptcy sense, and, therefore, that any plan which deprives the stockholders of the equity resulting from this "solvency" is an unfair plan which cannot be confirmed. This contention is based on a fundamental misconception of the purposes and provisions of the Bankruptcy Act (11 U. S. C. §205).

No part of these proceedings has been based upon any question of solvency in the bankruptcy sense. The original petition of the debtor only alleged "that it is unable to meet its debts as they mature" (R. 26). The Interstate Commerce Commission has made no finding that the debtor was insolvent, instead, its finding (R. 3700) was that stockholders could not participate in the reorganized com-

pany because their equities "have no value". The District Court, in its opinion approving the plan, made no specific finding relating to the debtor's solvency, but after discussing the matter, said "the Court is satisfied * * * that the findings made by the Commission * * * including its findings as to debtor's prospective earning power, the valuation and capitalization permissible for the purposes of this reorganization are supported by the entire record, * * *." (R. 5211-5212).

This procedure is within the clear intent of the statute that the permissible capitalization of the reorganized Company in railroad reorganizations is based primarily upon earning power. Section 77(e) provides (11 U. S. C. §205 (e)):

> "*Provided*, That submission to any class of stockholders shall not be necessary if the Commission shall have found, and the judge shall have affirmed the finding, (a) that at the time of the finding the corporation is insolvent, or that at the time of the finding the equity of such class of stockholders has no value, * * *."

The last clause, above quoted, has no meaning if it were to be construed as a mere repetition of the preceding clause as to insolvency.

The finding that an equity has no value is based upon earning power. This Court has so interpreted the act in *Group of Institutional Investors v. Chicago, Milwaukee, St. Paul & Pacific Railroad Company, supra*, 1. c. 540-541, as follows:

> "We recently stated in *Consolidated Rock Products Co. v. DuBois*, * * * *supra*, in connection with a reorganization of an industrial company, that the 'criterion of earning capacity is the essential one if the industry is to be freed from the heavy hand of past errors, miscalculations or disaster, and if the allocation of securities among the various claimants is to be fair and equitable.' p. 526. That is equally applicable to a rail-

road reorganization. * * * The basic question in a valuation for reorganization purposes is how much the enterprise in all probability can earn. Earning power was the primary test in former railroad reorganizations under equity receivership proceedings. *Temmer v. Denver Tramway Co.*, (CCA 8th) 18 F. 2d. 226, 229; *New York Trust Co. v. Continental & C. Trust & Sav. Bank*, (CCA 8th) 26 F. 2d. 872, 874. The reasons why it is the appropriate test are apparent. A basic requirement of any reorganization is the determination of a capitalization which makes it possible not only to respect the priorities of the various classes of claimants but also to give the new company a reasonable prospect for survival. See Commissioner Eastman dissenting, Chicago, M. & St. P. Reorganization, 131 I. C. C. 673, 705. Only 'meticulous regard for earning capacity' (*Consolidated Rock Products Co. v. DuBois, supra*, p. 525) can afford the old security holders protection against a dilution of their priorities and can give the new company some safeguards against the scourge of overcapitalization . Disregard of that method of valuation can only bring, as stated by Judge Evans for the court below, 'a harvest of barren regrets'. 124 F. 2d. p. 765. Certainly there is no constitutional reason why earning power may not be utilized as the criterion for determining value for reorganization purposes. And it is our view that Congress when it passed Section 77 made earning power the primary criterion. The limited extent to which Section 77(e) provides that reproduction cost, original cost, and actual investment may be considered indicates that (apart from doubts concerning constitutional power to disregard them) such other valuations were not deemed relevant under Section 77 any more than under Section 77 B 'except as they may indirectly bear on earning capacity'. *Consolidated Rock Products Co. v. DuBois, supra*, p. 526."

If, therefore, earning power is the criterion, it is certainly conceivable that there might be situations where a highly solvent company produced only small returns, and

could only produce such small returns. In such instances, the application of the correct criterion of earnings might wipe out a value which would be obtainable by the equity owners on a liquidation if the assets were saleable at or near their book values. Such result would be necessary if the business was to be continued at all. The reverse situation, where a liquidation would produce nothing for the equity owners but where there were foreseeable earnings allocable to such equity, has been considered by this Court, and the equity holders allotted participation in the reorganized company. See *Otis & Co. v. Securities & Exchange Commission*, 323 U. S. 624 (1945).

As pointed out above, the base on which these proceedings were instituted and conducted, was that the debtor was unable to meet its debts as they mature. Despite the war earnings and the changes in the debtor's financial condition, this situation still exists. Appendix A to the debtor's petition herein shows net current assets of $22,090,504 out of which, of course, the debtor must retain a sufficient sum for working capital. Against this, there are overdue debts of $38,303,211 made up as follows:

First Terminal & Unifying Mortgage Bonds[1]	$ 8,063,000
Chase National Bank Note	3,500,000
Mississippi Valley Trust Company Note	1,000,000
Reconstruction Finance Corporation Note (bought by Southern Pacific)	17,882,250
Stephenville N. & S. T. R. Co. Bonds	2,234,903[2]
Central Ark. & E. R. Co. Bonds	932,232[2]
Total interest in default	4,690,826
	$38,303,211

[1] The maturity of these bonds was accelerated by Guaranty Trust Company, Trustee.

[2] These figures are from the opinion of the Circuit Court of Appeals, below, 157 F. 2d. 337, 402-403.

Thus, for two reasons, whether or not this debtor is solvent in the bankruptcy sense, is irrelevant and immaterial. First, these proceedings are based on inability to meet debts as they mature, a condition which still exists. Second, regardless of solvency, any capitalization must be one which the earnings can support.

POINT IV.

The so-called "changed conditions" were in the contemplation of the Interstate Commerce Commission at the time it formulated the plan of reorganization.

The three petitioners contend that changed conditions, in the form of "solvency" of the debtor and increased earnings make the plan inequitable now, and require its referral back to the Interstate Commerce Commission. Their point relative to solvency was discussed under Point III above, which discussion will not be repeated. As to the increased earnings, none of the petitioners contend that the plan was inequitable for that reason at the time the plan was formulated by the Commission or certified to the District Court.

The Bankruptcy Act provides (11 U. S. C. §205(e)):

> "*Provided,* That submission to any class of stockholders shall not be necessary if the Commission shall have found, and the judge shall have affirmed the finding, (a) that *at the time of the finding*[3] the corporation is insolvent, or that *at the time of the finding* the equity of such class of stockholders has no value, * * *.
>
> "*Provided further,* That submission to any class of creditors shall not be necessary if the Commission shall have found, and the judge shall have affirmed the finding, that * * * *at the time of the finding* the interests of such class of creditors have no value, * * *."

[3] All italics in quotations herein are supplied unless the contrary is indicated.

Thus, the Bankruptcy Act provides that the cut-off date for determining the interest of a claimant, whether a creditor or a stockholder, is *the time of the finding* thereon by the Commission. Thus the cut-off date is fixed by the statute at a time when the reorganization is still before the Interstate Commerce Commission. The District Court is not required by the Bankruptcy Act to make a new finding. All it may do is affirm "the finding, * * * that at the time of the finding the equity of such class of stockholders has no value, * * *." The petitioners herein do not attack the finding of the Interstate Commerce Commission at the time the finding was made. Therefore the basis for their contentions arising out of "changed conditions" must arise out of reliance upon the general equity powers inherent in a court of bankruptcy.

Such inherent powers are also recognized by the Bankruptcy Act (11 U. S. C. §205(e)):

> "Upon the certification of a plan by the Commission to the court, * * * such parties shall file, * * * detailed and specific objections in writing to the plan *and their claims for equitable treatment.*"

Such is also the necessary effect of the decisions of this Court in *Ecker v. Western Pacific Railroad Corporation, Supra; Group of Institutional Investors v. Chicago, Milwaukee, St. Paul & Pacific Railroad Co., supra;* and *Reconstruction Finance Corporation v. Denver & Rio Grande Western Railroad Company, supra.*

In the *Western Pacific* Case, this Court considered the contention of changed conditions, but decided that the claimants for equitable treatment had not shown any such changed conditions as would justify disapproval of the Commission plan (1. c. 509):

> "The Commission's forecast was made with knowledge and not in disregard of past fluctuations of in-

> come, in war and in peace. On the showing as to changed conditions made before the District Court, there was no basis for a disapproval of the Commission plan as unfair to the junior equities. The further evidence of increased earnings, placed in the record by the stipulations, does not lead us to reject the Commission's plan."

In the *Milwaukee* Case, the contention was similarly handled (1. c. 543-544):

> "We agree with the Circuit Court of Appeals that no sufficient showing of changed circumstances has been made which requires the District Court to return the plan to the Commission for reconsideration. * * * As we have noted, the Commission conceived as its responsibility the devising of a plan which would serve 'as a basis for the company's financial structure for the indefinite future.' We cannot assume that the figures of war earnings could serve as a reliable criterion for that 'indefinite future'. As some of the bondholders point out, the bulge of war earnings per se is unreliable for use as a norm unless history is to be ignored; and numerous other considerations, present here as in former periods, make them suspect as a standard for any reasonably likely future normal year. * * * In view of these considerations *we cannot say that the junior interests have carried the burden which they properly have* of showing that subsequent events make necessary a rejection of the Commission's plan."

Those two cases, as the present one, involved attacks upon the approval of a plan, and the reliance upon the general equity power of the court is not clearly pointed up. However, the *Denver & Rio Grande* Case was squarely bottomed on that power.

In that case, the order subject to review was one confirming a plan which had not received the required number of acceptances, such confirmation being based upon a find-

ing that such non-assenting creditors were not "reasonably justified" (11 U. S. C. §205(e)) in failing to accept the plan. In determining whether such creditors were "reasonably justified" it was necessary for the court, in the absence of statutory guidance, to exercise its general equity powers. In upholding the confirmation of the plan, this Court said (1. c. 90 L. ed. 1148):

> "Assuming that the courts, as courts with equity powers in a bankruptcy matter, might set aside a plan, fair and equitable when adopted by the Commission, merely on account of subsequent changes in economic conditions of the region or the nation, it should not be done when the changes are of the kind that were envisaged and considered by the Commission in its deliberations upon or explanations of the plan."

This Court, however, found that there were no changed conditions which had not been envisaged by the Commission, and therefore held that the non-acceptance of the plan was not reasonably justified.

The position of the petitioners herein, therefore, must be that the Interstate Commerce Commission, in March of 1942 (the date of its Supplemental Report), failed to envisage the extent of the war and post-war earnings of the debtor, and the changes made and which can be made as a result of the large accumulation of earnings. None of the petitioners have stated what must be their basic assumption, i. e., that the increased earnings and their results are so great as conclusively to show that the Commission could not possibly have envisaged them. None of them adduces any facts or arguments to show that the Commission so failed.

In the *Denver & Rio Grande* Case, *supra*, this Court said (1. c. 90 L. ed. 1148-1150):

> "We have pointed out in the section of this opinion dealing with the allocations of the securities that a

part of the compensation to senior claimants for their loss of position was the opportunity to participate in war earnings. This was understood by the District Court and the Commission. Accumulations of cash beyond operating fund needs are in the same category. * * *

"The error of the Circuit Court in its holding set out above lies in its assumption that the senior bondholders were paid in full by the securities allotted to them without also accepting the determination of the Commission that the assets represented as of January 1, 1943, and all subsequent earnings were a part also of the common stock that was awarded the senior bondholders. * * *

"Under our determination that the creditors who received common stock were compensated partly by the assets and future earnings, it is obvious that the use of such assets to retire senior claims is a part of the normal and expected increment from holdings of common stock. * * * When proposed capitalization is being planned on earnings, a reduction of senior capital without reduction of estimated earnings increases possible junior capital within the scheme. When the reduction of senior capital takes place after the adoption of the plan by the use of anticipated earnings or existing cash, there can be no such readjustment of junior participation because assets in the balance sheet at the adoption of the plan and subsequent earnings are, as we have pointed out, for the benefit of the stockholders in the new company so that through these common stock advantages these new stockholders may be compensated for their loss of payment in full in cash."

This policy was reemphasized and reaffirmed by this Court in the second appeal in the *Denver & Rio Grande* Case (*Insurance Group Committee v. The Denver & Rio Grande Western Railroad Company*, ... U. S. ....., (February 3, 1947), as follows:

"The Commission made no finding that the cash value of the securities allocated to the senior creditors

paid them in full. To justify the change of position of creditors from fully secured to partially secured, creditors were given opportunities to participate in profits through common stock ownership *with a chance at larger earnings than the Commission's forecast anticipated*. We held the priority rule was satisfied by this type of allocation. This was explained by our decision on the last review. Slip opinion, *supra*, p. 15. The debtor has made no allegation, either in this effort for re-examination or before, that the existing cash value of the securities allotted any creditor has ever aggregated the amount of the creditor's claim against the debtor. We think the absence of such an allegation, of itself, demonstrates that the plan is not, because of excessive interest, unfair to the debtor or those for whom it is allowed to appear.

"Until it can be contended with some show of reasonableness that the creditors senior to the creditors and stockholders whom the debtor represents here have received more in value than the face of their claims, the debtor's insistence on a re-examination of the plan is without substantial support."

The petitioners have submitted no facts to show either (a) that the war and post-war earnings and their results were not, and could not have been, envisaged by the Commission, or (b) stating it differently, that the war and post-war earnings and their results are such as to require the court to exercise its general equity power to set aside a plan, fair when adopted, on the grounds that events subsequent to its adoption make it grossly inequitable, or (c) that the cash value of the securities allocated to the senior creditors paid them in full. Rather, the record supports the plan of the Commission. Over a twenty-four year period, the average earnings of the debtor would only have made available for the proposed common stock to be issued under

the plan, annual earnings of approximately $7.82 per share.[4] Such earnings would hardly seem to justify, much less *require*, such exercise of a general equitable power and further, seem to indicate that the Commission must have envisaged the large war and post-war earnings.

Under the plan, the earliest maturity of any debt of any consequence is that of the First Mortgage Certificates in 1989, (the new Consolidated Mortgage Bonds are not to mature until 1992). Hence, the Interstate Commerce Commission must have been considering a financial structure

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[4] This computation makes no adjustments (a) to conform any of the Debtor's figures to those authorized by the Interstate Commerce Commission, (b) for increase in Federal income taxes had the Debtor's interest charges been the lower amounts called for by the plan, nor (c) for the recent rate increase. The figures for the years 1923-1944, inclusive are from R. 5657, for the year 1945, from R. 5727, and for 1946 from the estimate on page 11 of the petition herein of Southern Pacific Company. The figure of Undisturbed fixed charges eliminates the interest on the Railroad Credit Corporation notes.

1923	$5,929,628	1935	$2,695,111
1924	5,028,749	1936	3,333,243
1925	5,057,460	1937	2,304,505
1926	5,072,628	1938	2,088,299
1927	4,692,923	1939	1,199,158
1928	4,382,449	1940	2,860,221
1929	3,714,052	1941	7,495,940
1930	2,380,379	1942	8,692,636
1931	2,710,861	1943	10,562,547
1932	(125,857)	1944	11,133,608
1933	1,840,184	1945	7,001,641
1934	2,024,891	1946	7,000,000

Average income of the twenty-four years 1923 to 1946, inclusive		$4,544,802
Less charges under plan (R. 3785, 3797, 3798):		
Undisturbed fixed charges	$872,970	
New mortgage interest	587,501	
Capital fund	500,000	
Sinking fund	179,763	
Preferred dividends	937,505	3,077,739
Available for common dividends		$1,467,063
Earnings per common share		$7.82

which would weather the possible vissisitudes of almost half a century, and it might well contemplate further wars and major depressions during that period. A capitalization which, over a twenty-four year period including a boom, a major depression and a war boom, only averages $7.82 per share for the common stock, supports the wisdom and experience of the Interstate Commerce Commission.

The petitioners urge that because the plan in this reorganization has been criticized before Congress, this Court should order the plan referred back to the Interstate Commerce Commission. In the first *Denver & Rio Grande* Case, *supra*, this Court restated its duty as one to follow the dictates of Congress and not to attempt to anticipate Congressional action. This Court said (1. c. 90 L. ed. 1139-1141):

> "The agencies employed by Congress to accomplish reorganizations under Section 77 were the Interstate Commerce Commission and the courts. The answer reached by Congress was that the experience and judgment of the Commission must be relied upon for final determinations of value and of matters affecting the public interest, subject to judicial review to assure compliance with Constitutional and statutory requirements. * * *

(1. c. 90 L. ed. 1142-1143):

> "* * * Our constructions of the chief provisions of the section were handed down in March, 1943. Although the results of reorganizations under the section as thus construed, have been criticized as unfortunate and changes have been suggested, no different legislation has been enacted. Indeed a different method for reorganization, enacted in 1939 and designed to meet the requirements of railroads not in need of financial reorganization of the character provided by Section 77 but only of an opportunity for voluntary adjustments with their creditors, terminated on July 31, 1940, and a comparable provision made in 1942 was allowed to

> lapse on November 1, 1945.[5] This situation leaves clear the duty of the agencies of the Government entrusted with the handling of reorganizations under Section 77, including this Court, to administer its provisions according to their best understanding of the purposes of Congress as expressed in the words of Section 77 read in the light of the contemporaneous discussion in Congress."

The obligation of this Court to ignore public pressure and to act under the existing law, and to refrain from attempting to anticipate Congressional action, was reaffirmed by this Court in *Insurance Group Committee v. The Denver & Rio Grande Western Railroad Company*, ... U. S. ..... (February 3, 1947), where it said:

> "* * * Nor do we see that the action of Congress in passing S. 1253, on July 31, 1946, should persuade us to require a stay to await further enactments that might affect this reorganization. It was vetoed. President's Memorandum of Disapproval, August 13, 1946. Our understanding of our duties under the Railroad Reorganization Act, in the face of strong criticism of its provisions, was expressed in the former review of this plan, slip opinion, p. 9. It need not be repeated. We must continue to act under the now existing law. Whether or not changes may be made that will affect this reorganization, we do not know."

In addition, this Court has expressed its appreciation of the Congressional purpose to eliminate delays in rail-

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[5] Similar legislation, embodied in S. 249, is now before Congress. This proposed law does not apply to reorganizations of railroads now in receivership proceedings or under Section 77, and thus differs materially from the vetoed legislation discussed at length by Mr. Justice Frankfurter in his dissent in *Insurance Group Committee v. The Denver & Rio Grande Western Railroad Company*, ... U. S. ..... (February 3, 1947). Furthermore, this difference would seem to support the decision of the majority in that case that this Court must continue to act under the now existing law. S. 249 is printed as Appendix B hereto.

road reorganizations. As pointed out above, this debtor has been in reorganization more than twelve years, including more than five years before the Interstate Commerce Commission. If these proceedings are referred back to the Commission, twelve years will in large part be lost, with no assurance that some litigious person will not again unduly delay these proceedings.

Another result of such referral might well be a plan formulated by the Interstate Commerce Commission during abnormally good years, but which would reach this Court during depression years, and therefore be referred back to the Interstate Commerce Commission a third time. The only escape of the debtor from such a vicious circle would be a dismissal under Section 77(g) (11 U. S. C. §205 (g)), which might leave the debtor still unable to meet its debts and still unreorganized.

CONCLUSION.

It is respectfully submitted that a writ of certiorari should not issue.

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Dated: February 11, 1947.

APPENDIX A.

11 U. S. C. §205 (d)(e) and (g):

"(d) The debtor, after a petition is filed as provided in subsection (a) of this section, shall file a plan of reorganization within six months of the entry of the order by the judge approving the petition as properly filed, or if heretofore approved, then within six months of the effective date of this Act, and not thereafter unless such time is extended by the judge from time to time for cause shown, no single extension at any one time to be for more than six months. Such plan shall also be filed with the Commission at the same time. Such plans may likewise be filed at any time before, or with the consent of the Commission during, the hearings hereinafter provided for, by the trustee or trustees, or by or on behalf of the creditors being not less than 10 per centum in amount of any class of creditors, or by or on behalf of any class of stockholders being not less than 10 per centum in amount of any such class, or with the consent of the Commission by any party in interest. After the filing of such a plan, the Commission, unless such plan shall be considered by it to be prima facie impracticable, shall, after due notice to all stockholders and creditors given in such manner as it shall determine, hold public hearings, at which opportunity shall be given to any interested party to be heard, and following which the Commission shall render a report and order in which it shall approve a plan, which may be different from any which has been proposed, that will in its opinion meet with the requirements of subsections (b) and (e) of this section, and will be compatible with the public interest; or it shall render a report and order in which it shall refuse to approve any plan. In such report the Commission shall state fully the reasons for its conclusions.

The Commission may thereafter, upon petition for good cause shown filed within sixty days of the date of its order, and upon further hearings if the Commission shall deem

necessary, in a supplemental report and order modify any plan which it has approved, stating the reasons for such modification. The Commission, if it approves a plan, shall thereupon certify the plan to the court together with a transcript of the proceedings before it and a copy of the report and order approving the plan. No plan shall be approved or confirmed by the judge in any proceeding under this section unless the plan shall first have been approved by the Commission and certified to the court.

"(e) Upon the certification of a plan by the Commission to the court, the court shall give due notice to all parties in interest of the time within which such parties may file with the court their objections to such plan, and such parties shall file, within such time as may be fixed in said notice, detailed and specific objections in writing to the plan and their claims for equitable treatment. The judge shall, after notice in such manner as he may determine to the debtor, its trustee or trustees, stockholders, creditors, and the Commission, hear all parties in interest in support of, and in opposition to, such objections to the plan and such claims for equitable treatment. After such hearing, and without any hearing if no objections are filed, the judge shall approve the plan if satisfied that: (1) It complies with the provisions of subsection (b) of this section, is fair and equitable, affords due recognition to the rights of each class of creditors and stockholders, does not discriminate unfairly in favor of any class of creditors or stockholders, and will conform to the requirements of the law of the land regarding the participation of the various classes of creditors and stockholders; (2) the approximate amounts to be paid by the debtor, or by any corporation or corporations acquiring the debtor's assets, for expenses and fees incident to the reorganization, have been fully disclosed so far as they can be ascertained at the date of such hearing, are reasonable, are within such maximum limits as are fixed by the Commission, and are within such maximum limits to be subject to the approval of the judge; (3) the plan provides for the payment of all costs of administration and all other allowances made or to be made by the judge,

except that allowances provided for in subsection (c), paragraph (12) of this section, may be paid in securities provided for in the plan if those entitled thereto will accept such payment, and the judge is hereby given power to approve the same.

"If the judge shall not approve the plan, he shall file an opinion, stating his conclusions and the reason therefor, and he shall enter an order in which he may either dismiss the proceedings, or in his discretion and on motion of any party in interest refer the proceedings back to the Commission for further action, in which event he shall transmit to the Commission a copy of any evidence received. If the proceedings are referred back to the Commission, it shall proceed to a reconsideration of the proceedings under the provisions of subsection (d) of this section. If the judge shall approve the plan, he shall file an opinion, stating his conclusions and the reasons therefor, and enter an order to that effect, and shall send a certified copy of such opinion and order to the Commission. The plan shall then be submitted by the Commission to the creditors of each class whose claims have been filed and allowed in accordance with the requirements of subsection (c) of this section, and to the stockholders of each class, and/or to the committees or other representatives thereof, for acceptance or rejection, within such time as the Commission shall specify, together with the report or reports of the Commission thereon or such a summarization thereof as the Commission may approve, and the opinion and order of the judge: *Provided,* That submission to any class of stockholders shall not be necessary if the Commission shall have found, and the judge shall have affirmed the finding, (a) that at the time of the finding the corporation is insolvent, or that at the time of the finding the equity of such class of stockholders has no value, or that the plan provides for the payment in cash to such class of stockholders of an amount not less than the value of their equity, if any, or (b) that the interests of such class of stockholders will not be adversely and materially affected by the plan, or (c) that the debtor has pursuant to authorized corporate

action accepted the plan and its stockholders are bound by such acceptance: *Provided further,* That submission to any class of creditors shall not be necessary if the Commission shall have found, and the judge shall have affirmed the finding, that the interests of such class of creditors will not be adversely and materially affected by the plan, or that at the time of the finding the interests of such class of creditors have no value, or that the plan provides for the payment in cash to such class of creditors of an amount not less than the value of their interests. For the purpose of this section the acceptance or rejection by any creditor or stockholder shall be in writing, executed by him or by his duly authorized attorney, committee, or representative. If the United States of America, or any agency thereof, or any corporation (other than the Reconstruction Finance Corporation) the majority of the stock of which is owned by the United States of America, is a creditor or stockholder, the interests or claims thereof shall be deemed to be affected by the plan, and the President of the United States, or any officer or agency he may designate, is hereby authorized to act in respect of the interests or claims of the United States or of such agency or other corporation. The expense of such submission shall be certified by the Commission and shall be borne by the debtor's estate. The Commission shall certify to the judge the results of such submission.

"Upon receipt of such certification, the judge shall confirm the plan if satisfied that it has been accepted by or on behalf of creditors of each class to which submission is required under this subsection holding more than two-thirds in amount of the total of the allowed claims of such class which have been reported in said submission as voting on said plan, and by or on behalf of stockholders of each class to which submission is required under this subsection holding more than two-thirds of the stock of such class which has been reported in said submission as voting on said plan; and that such acceptances have not been made or procured by any means forbidden by law: *Provided,* That, if the plan has not been so accepted by the creditors and

stockholders, the judge may nevertheless confirm the plan if he is satisfied and finds, after hearing, that it makes adequate provision for fair and equitable treatment for the interests or claims of those rejecting it; that such rejection is not reasonably justified in the light of the respective rights and interests of those rejecting it and all the relevant facts; and that the plan conforms to the requirements of clauses (1) to (3), inclusive, of the first paragraph of this subsection (e): *Provided further,* That if, in any reorganization proceeding under this section, the United States is a creditor on claims for taxes or customs duties (whether or not the United States has any other interest in, or claim against, the debtor, as creditor or stockholder), no plan which does not provide for the payment thereof shall be confirmed by the judge except upon the acceptance certified to the court, of a lesser amount by the President of the United States or the officer or agency designated by him pursuant to the provisions of the preceding paragraph hereof: *Provided further,* That if the President of the United States or such officer or agency shall fail to accept or reject such lesser amount for more than ninety days after receipt of written notice so to do from the court, accompanied by a certified copy of the plan, the consent of the United States insofar as its claims for taxes or customs duties are concerned shall be conclusively presumed. If the judge shall confirm the plan, he shall enter an order and file an opinion with a statement of his conclusions and his reasons therefor. If the judge shall not confirm the plan, he shall file an opinion, with a statement of his conclusions and his reasons therefor, and enter an order in which he shall either dismiss the proceedings, or, in his discretion and on the motion of any party in interest, refer the case back to the Commission for further proceedings, including the consideration of modifications of the plan or the proposal of new plans. In the event of such a reference back to the Commission, the proceedings with respect to any modified or new plan shall be governed by the provisions of this section in like manner as in an original proceeding hereunder.

"If it shall be necessary to determine the value of any property for any purpose under this section, the Commission shall determine such value and certify the same to the court in its report on the plan. The value of any property used in railroad operation shall be determined on a basis which will give due consideration to the earning power of the property, past, present, and prospective, and all other relevant facts. In determining such value only such effect shall be given to the present cost of reproduction new and less depreciation and original cost of the property, and the actual investment therein, as may be required under the law of the land, in light of its earning power and all other relevant facts.

"(g) If in the light of all the existing circumstances there is undue delay in a reasonably expeditious reorganization of the debtor, the judge, in his discretion, shall, on motion of any party in interest or on his own motion, after hearing and after consideration of the recommendation of the Commission, dismiss the proceedings. Upon the filing of such an order of dismissal, all right, title, or interest of the trustee or trustees shall vest by operation of law in the debtor unless otherwise provided by such order."

APPENDIX B.

80TH CONGRESS
1ST SESSION

S. 249

IN THE SENATE OF THE UNITED STATES

JANUARY 15, 1947

MR. WHITE (by request) introduced the following bill; which was read twice and referred to the Committee on Interstate and Foreign Commerce

A BILL

To amend the Interstate Commerce Act, as amended, and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That it is hereby declared to be in aid of the national transportation policy of the Congress, as set forth in the preamble of the Interstate Commerce Act, as amended, in order to promote the public interest in avoiding the deterioration of service and the interruption of employment which inevitably attend the threat of financial difficulties and which follow upon financial collapse and in order to promote the public interest in increased stability of values of railroad securities with resulting greater confidence therein of investors, to assure, insofar as possible, continuity of sound financial condition of common carriers subject to part I of said Act, and to enable said common carriers, insofar as possible, to avoid prospective financial difficulties, inability to meet debts as they mature, and insolvency. To assist in

accomplishing these ends and because certain classes of the obligations of such carriers are in the usual case held by a very large number of holders, and further to enable modification and reformation of provisions of the aforesaid classes of obligations and of provisions of the instruments pursuant to which they are issued or by which they are secured in cases where such modification and reformation shall have become necessary or desirable in the public interest in order to avoid obstruction to or interference with the economical, efficient, and orderly conduct by such carriers of their affairs, it is deemed necessary to provide means, in the manner and with the safeguards herein provided, for the alteration and modification, without the assent of every holder thereof, of the provisions of such classes of obligations and of the instruments pursuant to which they are outstanding or by which they are secured.

Part I of the Interstate Commerce Act, as amended, is amended by adding after section 20a the following new section:

"20b. (1) It shall be lawful (any express provision contained in any mortgage, indenture, deed of trust, or other instrument to the contrary notwithstanding), with the approval and authorization of the Commission, as provided in paragraph (2) hereof, for a carrier as defined in section 20a (1) of this part (other than a carrier in equity receivership or in process of reorganization under section 77 of the Bankruptcy Act) to alter or modify (a) any provision of any class or classes of its bonds, notes, debentures, or other evidences of indebtedness (whether secured, unsecured, matured, or unmatured) issued under any mortgage, indenture, deed of trust, or other instrument of like nature, such bonds, notes, debentures, or other evidences of indebtedness being hereinafter in this section sometimes called 'obligations'; (b) any provision of any mortgage, indenture, deed of trust, or other instrument pursuant to which any class of its obligations shall have been issued or by which any class of its obligations is secured: *Provided*, That the provisions of this section shall not apply to any equipment-trust certi-

ficates in respect of which a carrier is obligated, or to any evidences of indebtedness of a carrier the payment of which is secured in any manner solely by equipment, or to any instrument, whether an agreement, lease, conditional-sale agreement, or otherwise, pursuant to which such equipment-trust certificates or such evidences of indebtedness shall have been issued or by which they are secured.

"(2) Whenever an alteration or modification is proposed under paragraph (1) hereof, the carrier seeking authority therefor shall, pursuant to such rules and regulations as the Commission shall prescribe, present an application to the Commission. Upon presentation of any such application, the Commission may, in its discretion, but need not, as a condition precedent to further consideration, require the applicant to secure assurances of assent to such alteration or modification by holders of such percentage of the aggregate principal amount outstanding of the obligations affected by such alteration or modification as the Commission shall in its discretion determine. If the Commission shall not require the applicant to secure any such assurance, or when such assurances as the Commission may require shall have been secured, the Commission shall set such application for public hearing and the carrier shall give such notice of such hearing in such manner, by advertisement or otherwise, as the Commission may find practicable and may direct, to holders of such of its classes of securities and to such other persons in interest as the Commission shall determine to be appropriate and shall direct. If the Commission, after hearing, in addition to making (in any case where such alteration or modification involves an issuance of securities) the findings required by paragraph (2) of section 20a, shall find that, subject to such terms and conditions and with such amendments as it shall determine to be just and reasonable, the proposed alteration or modification—

"(a) is within the scope of paragraph (1);

"(b) will be in the public interest;

"(c) will be in the best interests of the carrier, of each class ot its stockholders, and of the holders of each class of its obligations affected by such modification or alteration; and

"(d) will not be adverse to the interests of any creditor of the carrier not affected by such modification or alteration

then (unless the applicant carrier shall withdraw its application) the Commission shall cause the carrier, in such manner as it shall direct, to submit the proposed alteration or modification (with such terms, conditions, and amendments, if any) to the holders of each class of its obligations affected thereby, for acceptance or rejection. All letters, circulars, advertisements, and other communications, and all financial and statistical statements, or summaries thereof, to be used in soliciting the assents or the opposition of such holders shall, before being so used, be submitted to the Commission for its approval as to correctness and sufficiency of the material facts stated therein. If the Commission shall find that as a result of such submission the proposed alteration or modification has been assented to by the holders of at least 75 per centum of the aggregate principal amount outstanding of each class of obligations affected thereby (or in any case where 75 per centum thereof is held by fewer than twenty-five holders, such larger percentage, if any, as the Commission may determine to be just and reasonable and in the public interest), the Commission shall enter an order approving and authorizing the proposed alteration or modification upon the terms and conditions and with the amendments, if any, so determined to be just and reasonable. Such order shall make provision as to the time when such alteration or modification shall become and be binding, which may be upon publication of a declaration to that effect by the carrier, or otherwise, as the Commission may determine. Any alteration or modification which shall become and be binding pursuant to the approval and authority of the Commission hereunder shall be binding upon each holder of any obligation of the carrier of each class affected by such alteration

or modification, and upon any trustee or other party to any instrument under which any such class of obligations shall have been issued or by which it is secured, and when any alteration or modification shall become and be binding the rights of each such holder and of any such trustee or other party shall be correspondingly altered or modified.

"(3) For the purposes of this section a class of obligations shall be deemed to be affected by any modification or alteration proposed only (a) if a modification or alteration is proposed as to any provision of such class of obligations, or (b) if any modification or alteration is proposed as to any provision of any instrument pursuant to which such class of obligations shall have been issued or shall be secured: *Provided*, That in any case where more than one class of obligations shall have been issued, and be outstanding or shall be secured pursuant to any instrument, any alteration or modification proposed as to any provision of such instrument which does not relate to all of the classes of obligations issued thereunder, shall be deemed to affect only the class or classes of obligations to which such alteration or modification is related. For the purpose of the finding of the Commission referred to in paragraph (2) of this section as to whether the required percentage of the aggregate principal amount outstanding of each class of obligations affected by any proposed alteration or modification has assented to the making of such alteration or modification, any obligation which secures any evidence or evidences of indebtedness of the carrier or of any company controlling or controlled by the carrier shall be deemed to be outstanding unless the Commission in its discretion determines that the proposed alteration or modification does not materially affect the interests of the holder or holders of the evidence or evidences of indebtedness secured by such obligation. Whenever any such pledged obligation is, for said purposes, to be deemed outstanding, assent in respect of such obligations, as to any proposed alteration or modification, may be given only (any express or implied provision in any mortgage, indenture, deed of trust, note, or other instrument to the contrary notwithstanding) as

follows: (a) Where such obligation is pledged as security under a mortgage, indenture, deed of trust, or other instrument, pursuant to which any evidences of indebtedness are issued and outstanding, by the holders of a majority in principal amount of such evidences of indebtedness; or (b) where such obligation secures an evidence or evidences of indebtedness not issued pursuant to such a mortgage, indenture, deed of trust, or other instrument, by the holder or holders of such evidence or evidences of indebtedness; and in any such case the Commission, in addition to the submission referred to in paragraph (2) of this section, shall cause the carrier in such manner as it shall direct to submit the proposed alteration or modification (with such terms, conditions, and amendments, if any, as the Commission shall have determined to be just and reasonable) for acceptance or rejection, to the holders of the evidences of indebtedness issued and outstanding pursuant to such mortgage, indenture, deed of trust, or other instrument, or to the holder or holders of such evidence or evidences of indebtedness not so issued, and such proposed alteration or modification need not be submitted to the trustee of any such mortgage, indenture, deed of trust, or other instrument, but assent in respect of any such obligation shall be determined as hereinbefore in this section provided. For the purposes of this section an obligation or an evidence of indebtedness shall not be deemed to be outstanding if in the determination of the Commission the assent of the holder thereof to any proposed alteration or modification is within the control of the carrier or of any person or persons controlling the carrier.

"(4) (a) Any authorization and approval hereunder of any alteration or modification of a provision of any class of obligations of a carrier or of a provision of any instrument pursuant to which a class of obligations has been issued, or by which it is secured, shall be deemed to constitute authorization and approval of a corresponding alteration or modification of the obligation of any other carrier which has assumed liability in respect of such class of obligations as guarantor, endorser, surety, or otherwise: *Pro-*

vided, That such other carrier consents in writing to such alteration or modification of such class of obligations in respect of which it has assumed liability or of the instrument pursuant to which such class of obligations has been issued or by which it is secured and, such consent having been given, any such corresponding alteration or modification shall become effective, without other action, when the alteration or modification of such class of obligations or of such instrument shall become and be binding.

"(b) Any person who is liable or obligated contingently or otherwise on any class or classes of obligations issued by a carrier shall, with respect to such class or classes of obligations, for the purposes of this section, be deemed a carrier.

"(5) The authority conferred by this section shall be exclusive and plenary and any carrier, in respect of any alteration or modification authorized and approved by the Commission hereunder, shall have full power to make any such alteration or modification and to take any actions incidental or appropriate thereto, and may make any such alteration or modification and take any such actions, and any such alteration or modification may be made without securing the approval of the Commission under any other section of this Act or other paragraph of this section, and without securing approval of any State authority, and any carrier and its officers and employees and any other persons, participating in the making of an alteration or modification approved and authorized under the provisions of this section or the taking of any such actions, shall be, and they hereby are, relieved from the operation of all restraints, limitations, and prohibitions of law, Federal, State, or municipal, insofar as may be necessary to enable them to make and carry into effect the alteration or modification so approved and authorized, in accordance with the conditions and with the amendments, if any, imposed by the Commission. Any power granted by this section to any carrier shall be deemed to be in addition to and in modification of its powers under its corporate charter or under the laws of any State. The provisions of this section shall not

affect in any way the negotiability of any obligation of any carrier or of the obligation of any carrier which has assumed liability in respect thereto.

"(6) The Commission shall require periodical or special reports from each carrier which shall hereafter secure from the Commission approval and authorization of any alteration or modification under this section, which shall show, in such detail as the Commission may require, the action taken by the carrier in the making of such alteration or modification.

"(7) The provisions of this section are permissive and not mandatory and shall not require any carrier to obtain authorization and approval of the Commission hereunder for the making of any alteration or modification of any provision of any of its obligations or of any class thereof or of any provision of any mortgage, indenture, deed of trust, or other instrument, which it may be able lawfully to make in any other manner, whether by reason of provisions for the making of such alteration or modification in any such mortgage, indenture, deed of trust, or other instrument, or otherwise: *Provided*, That the provisions of paragraph (2) of section 20a, if applicable to such alteration or modification made otherwise than pursuant to the provisions of this section, shall continue to be so applicable.

"(8) The provisions of paragraph (6) of section 20a, except the provisions thereof in respect of hearings, shall apply to applications made under this section. In connection with any order entered by the Commission pursuant to paragraph (2) hereof, the Commission may from time to time, for good cause shown, make such supplemental orders in the premises as it may deem necessary or appropriate, and may by any such supplemental order modify the provisions of any such order, subject always to the requirements of said paragraph (2).

"(9) The provisions of subdivision (a) of section 14 of the Securities Exchange Act of 1934 shall not apply to any solicitation in connection with a proposed alteration or modification pursuant to this section.

"(10) The Commission shall have the power to make such rules and regulations appropriate to its administration of the provisions of this section as it shall deem necessary or desirable."

IN THE

Supreme Court of the United States

OCTOBER TERM, 1946

No. 879

SOUTHERN PACIFIC COMPANY,
a railroad corporation, Intervener,
Petitioner,

v.

BERRYMAN HENWOOD, as Trustee of St. Louis Southwestern Railway Company Lines, *et al.*,
Respondents.

No. 909

WALTER E. MEYER, Intervener,
Petitioner,

v.

BERRYMAN HENWOOD, as Trustee of St. Louis Southwestern Railway Company Lines, *et al.*,
Respondents.

No. 936

ST. LOUIS SOUTHWESTERN RAILWAY COMPANY,
a Corporation, Debtor,
Petitioner,

v.

BERRYMAN HENWOOD, as Trustee of St. Louis Southwestern Railway Company Lines, *et al.*,
Respondents.

BRIEF IN OPPOSITION TO PETITIONS FOR WRITS OF CERTIORARI

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Respondents.

BRIEF IN OPPOSITION TO PETITIONS FOR WRITS OF CERTIORARI TO THE CIRCUIT COURT OF APPEALS FOR THE 8TH CIRCUIT

The respondent, Guaranty Trust Company of New York, Trustee under the Debtor's First Terminal and Unifying Mortgage, files this brief in support of its prayer

that this Court deny the petitions of the Debtor, Southern Pacific Company and Walter E. Meyer requesting this Court to review the decision of the Circuit Court of Appeals for the 8th Circuit affirming the District Court's order approving a plan of reorganization for the St. Louis Southwestern Railway Company.

Opinions Below

District Court—53 F. Supp. 914 (R. 5183-5213)
Circuit Court of Appeals—152 F. (2d) 337 (R. 5559-5683)

Jurisdiction

The petitioners invoke the jurisdiction of this Court under Section 240(a) of the Judicial Code, as amended by the Act of February 13, 1925 (28 U. S. C. 347(a)), and Section 24(c) of the Bankruptcy Act (11 U. S. C. Sec. 47(c)).

The Property Involved

The St. Louis Southwestern Railway system lines comprise a group of railroads operating with main lines and branches from St. Louis, Missouri, and Memphis, Tennessee, to Shreveport, Louisiana, and points in Texas, the principal termini in Texas being at Corsicana and Fort Worth. The total road mileage operated by the system when the reorganization proceedings commenced was 1,749 miles. The Commission has found that traffic on the Debtor's main line is "highly competitive", and that its branch line traffic is "very light" (R. 3502). The Debtor must compete for traffic in the Southwest area with the Missouri-Pacific, St. Louis-San Francisco, Missouri-Kansas-Texas, and Kansas City Southern Railroads (R. 5581).

Statement of the Case

This proceeding was begun on December 12, 1935, when the Debtor filed its petition under Section 77 of the Bankruptcy Act. Similar petitions were filed by Debtor's three

subsidiaries, St. Louis Southwestern Railway Company of Texas, Central Arkansas and Eastern Railroad Company and Stephenville North and South Texas Railway Company. All objections to the Debtor's petition were overruled, and on January 3, 1936, one Trustee was appointed for the four Debtors.

Hearings on the plans of reorganization filed by the Debtor and others were begun March 16, 1937, and concluded April 24, 1937. The Examiner's Proposed Report was issued February 7, 1938, and objections thereon were argued before the Commission on May 16, 1938.

On January 10, 1939, the Commission reopened the proceedings for the purpose of receiving further evidence relating to the charges made by petitioner Meyer with respect to the effect upon the Debtor's earnings and assets of Southern Pacific's alleged diversion of traffic and failure to solicit traffic preferentially (R. 500-501). Thereafter, hearings were held for this sole purpose from May 5, 1939, to May 27, 1939, and from September 18, 1939, to September 30, 1939 (R. 529). At these hearings a vast amount of evidence, including hundreds of exhibits, was introduced (R. 529-2680, 2681-3055). The extensive record made at these hearings contained exhaustive studies of the earnings history of the Debtor upon which the Commission founded its finding as to the Debtor's prospective earning power.

On June 30, 1941, the Commission issued its initial Report and Order setting forth its plan of reorganization for the Debtor (R. 3495-3735; 249 I. C. C. 5). 131 pages of the Report are devoted to an elaborate consideration and rejection of the Meyer charges (R. 3547-3678). The plan reduced the Debtor's total capitalization from approximately $107,000,000 to $75,000,000 and fixed charges from approximately $3,400,000 to $1,500,000.

Petitions for modification of the plan were filed by various interveners, and on March 9, 1942, the Commission issued its Supplemental Report and Order, which modified its original plan in certain relatively minor respects but which reaffirmed the same so far as the present petitions

are concerned (R. 3736-3820; 252 I. C. C. 325). The modified plan was certified by the Commission to the District Court March 23, 1942 (R. 3494-3495).

From October 26, 1942, to November 5, 1942, hearings were held before the late Judge Davis upon objections to the certified plan at which additional evidence, including data as to the vastly increased earnings of the preceding two years, was presented (R. 4051-5136). The great bulk of such additional evidence related to the charges made by Walter E. Meyer against Southern Pacific (R. 4157-4199, 4202-4209, 4304-5136). Prior to the filing of briefs in support of the plan and objections thereto, Judge Davis died. The case was then referred to Judge Moore (R. 5138) who on April 23, 1943, entered an order directing a reargument on May 31, 1943, upon the case as submitted before Judge Davis, with all parties having the right to apply for leave to present additional testimony (R. 5181-5183). On February 8, 1944, the District Court filed an opinion and entered an order in which it rejected the contentions of the objectors and approved the certified plan.

Appeals were taken in March, 1944, to the Circuit Court of Appeals for the 8th Circuit by Southern Pacific, Walter E. Meyer, protective committees for the Stephenville and Central Arkansas bonds, respectively, and the Debtor, but due to the necessity of printing an inordinately voluminous record, argument was delayed until April 6, 1945. The Circuit Court handed down its decision August 26, 1946.

The Plan of Reorganization

Since the primary complaint of petitioners is not as to the terms of the Commission's plan of reorganization, but as to its alleged obsolete character, no elaborate discussion of the terms of the plan is required. It will suffice to say that the Commission's plan of reorganization for the Debtor calls for a capitalization of approximately $75,000,000 and fixed charges of approximately $1,500,000. The Debtor's

capitalization at the time it went into reorganization was $107,124,950, and fixed charges were, $3,379,341. (R. 3506, 3691)

Questions Presented

Only two questions are presented by the petitions for writs of certiorari:

First, whether changed conditions have occurred which were unanticipated by the Commission and which warrant review by this Court.

Second, whether the Commission has given proper consideration and disposition to petitioner Meyer's special charges of illegal control of the Debtor by Southern Pacific.

POINT I

The Petitioner's allegations regarding changed conditions do not warrant a return of the plan to the Commission.

In final analysis, the petitions for review by this Court of the fairness of the Commission's plan of reorganization for the Debtor are based primarily on the theory of changed conditions. This theory is rested upon two basic premises: one, that the reduction in the Debtor's defaulted interest obligations and other indebtedness and the increase in its current asset position has rendered the Debtor solvent; and two, that the Debtor has shown an earning power unanticipated by the Commission. Respondents believe that the first premise is contrary to the principles laid down by this Court and that the second can not be sustained on the meager additions to the record offered with the petitions, being a mere assertion by the petitioners as opposed to the expert judgment of the Commission.

The Petitioner's Theory Of Solvency Of The Debtor Is Unsound

All three petitioners rely heavily upon an alleged solvency of the Debtor in the bankruptcy sense resulting from cash distributions directed by the District Court and from

an improvement in the current asset position of the Debtor. As petitioner Southern Pacific states it: "The case for the present solvency of the Debtor is presented upon the basis of reduction in debt and improvement in current liquid assets" (Petition p. 8). Respondents believe that the fallacies in the position of petitioners lie in their disregard of the principles settled by this Court as to the effect of debt reduction and increase in current assets after the effective date of a plan, in their misconception of the significance of the Commission's proposed new total capitalization, and in their failure to analyze the effect of cash distributions under the plan.

(a) The decrease in debt and increase in current assets is for the benefit of the new security holders.

The effective date of the plan of reorganization in these proceedings is January 1, 1942. This Court has consistently held that it is for the Commission alone to determine the effective date of a plan of reorganization. *R. F. C.* v. *Denver & Rio Grande Western R. R. Co.*, 90 L. Ed. 1134, p. 1148; *Ecker* v. *Western Pacific R. Corp.*, 318 U. S. 448, 509; *Group of Institutional Investors* v. *Chicago, Milwaukee, St. Paul & Pacific R. Co.*, 318 U. S. 523, 546. The practical reason for this ruling was well stated by the Circuit Court of Appeals for the Second Circuit in *Old Colony Bondholders* v. *New York, New Haven & Hartford Railroad Company*, C. C. H. Bankruptcy Service, Par. 55,813 January 13, 1947, where the Court said (p. 58,527):

> "* * * As a practical matter some closing time must be set and it cannot be progressively postponed without reopening the issues and making new findings, with resulting new appeals. By the time these are finished conditions may again have changed, so on *ad inifinitum*. See *Interstate Commerce Comm.* v. *Jersey City, supra,* * * *"

Starting with this premise in the *Denver* case, this Court laid down the principles with respect to the effect of

reduction in debt and increase in current assets in a reorganization proceeding subsequent to the effective date which, respondents submit, govern the issues petitioners now seek to raise.

Petitioners' primary argument of changed conditions is founded on actual and assumed reductions of debt funded in the plan resulting from cash distributions made since the effective date of the plan. However, this same argument was made before this Court in the *Denver* case and rejected. There the effective date of the plan was January 1, 1943. Among the obligations of the Debtor funded in the plan as of that date were $2,758,330 of Rio Grande Junction Bonds. In addition, the plan provided for the assumption by the reorganized company of $5,758,000 of equipment obligations. Subsequent to the effective date the District Court authorized the Trustees to purchase the Junction Bonds and to pay off $1,218,000 of the equipment obligations. The capitalization of the new company was decreased proportionately. The Trustee for the most junior secured creditors protested that their participation should be increased by the amount of the debt reduction. The Circuit Court of Appeals for the Eighth Circuit accepted this argument and returned the plan to the District Court. This Court granted *certiorari* and reversed the Circuit Court on this point, stating (90 L. Ed. p. 1724):

> "* * * When the reduction of senior capital takes place after the adoption of the plan by use of anticipated earnings or existing cash, there can be no such readjustment of junior participation because assets in the balance sheet at the adoption of the plan and subsequent earnings are, as we have pointed out, for the benefit of the stockholders in the new company so that through these common stock advantages these new stockholders may be compensated for their loss of payment in full in cash. * * *."

So too in the instant case the reduction of debt after the adoption of the plan is for the benefit of the new security holders. As the table on page 9 of the petition of Southern

Pacific shows, precisely the same kind of debt reduction has occurred, in part at least, in this case as in the *Denver* proceeding. Here guaranteed obligations, viz. the Texarkana Union Station certificates, were purchased and a reduction in equipment obligations effected. A secured obligation of the Railroad Credit Corporation was also paid off, which was contemplated and provided for in the plan. As this Court held in the *Denver* case, the benefit of this action accrues to the new security holders. In addition, in this proceeding funds sufficient to pay interest arrears on certain senior securities, but not directed to be applied for that purpose, were disbursed. But this does not affect the application of the doctrine enunciated by this Court in the *Denver* case to this proceeding. Under that doctrine if these payments also effected a reduction in debt after the effective date such reduction must be for the benefit of the new security holders.

Furthermore, under an additional holding of this Court in the *Denver* case, it appears plain that the cash from which these payments were made belongs to the creditors provided for under the plan, because it was acquired subsequent to the plan's effective date. In the *Denver* proceeding this Court stated (90 L. Ed. p. 1146):

> "There is another important factor, corollary to stock ownership, to be noted in the Commission's allocation of these securities. *This factor is that the creditors who received common stock to make them whole obtained with that common stock an interest in all cash on hand or all cash that might be accumulated.* * * * Cash, material and supplies, as well as all other assets and all liabilities of the debtor were represented by the securities. If there is more cash on hand than needed, for taxes, expenses and proper improvements, it is at the disposal of the common stockholders. If money was used to pay indebtedness, there would be a corresponding reduction in the capital structure. * * *" [Emphasis supplied].

The Circuit Court of Appeals in that case had said (150 F. (2d) at p. 35):

> " • • • we cannot disregard the fact that these huge surpluses actually exist. Their existence is an accomplished fact. It is also obvious that surpluses will continue to pile up for a reasonable time yet to come. We think any plan which fails to take this into account and which gives the Senior Bondholders their claims in full by substantially delivering the road to them, and gives them the surplus cash actually on hand and further enables them to receive in addition the excess war profits which are reasonably sure to come, is inherently inequitable and unfair, so long as there are classes of creditors whose claims are not fully satisfied."

As to this holding, this Court stated (90 L. Ed. p. 1148):

> "In our judgment this holding is erroneous.
>
> The effective date of the plan was fixed by the Commission as January 1, 1943. This was in its power. The allocation of the securities took into consideration the interest of the secured claims to that date. *Any gain or any loss after that time was a benefit or an injury to the new common stockholders and then sometimes to security holders in positions senior to them.* Assuming that the courts, as courts with equity powers in a bankruptcy matter, might set aside a plan, fair and equitable when adopted by the Commission, merely on account of subsequent changes in economic conditions of the region or the nation, it should not be done when the changes are of the kind that were envisaged and considered by the Commission in its deliberations upon or explanations of the plan" (Emphasis supplied).

The Commission in this case, as in the *Denver* reorganization, did envisage the factors upon which petitioners rely in their claim of changed conditions. At the time of its Supplemental Report in this proceeding the Commission had before it the Trustee's statements (which are filed regularly with the Commission) showing earnings avail-

able for fixed charges for 1940 of $2,860,221 as compared with $1,119,158 for 1939 and $7,495,940 for 1941 as compared with both those earlier figures. The Trustee's reports also showed an increase in net current assets over those existing when the petition was filed from a deficit of $23,771,707 to an excess of current assets over current liabilities of $8,010,813 as of December 31, 1941 (Debtor's petition p. 9). The Commission was fully aware of the certainty of further increases resulting from war earnings. In the face of these facts the Commission said:

> "• • • the new securities, in the amounts in which they will be exchanged for the securities and claims of the old company, properly compensate the holders of the old securities for the rights given up by them, *by the rights and shares of earnings accorded them in the new company.* • • • " (Emphasis supplied.) R. 3776)

Thus, the Commission plainly contemplated in this proceeding, as in the *Denver* case, that a part of the compensation of creditors for their sacrifices consisted of participation in good earnings in prosperous years and an improvement in the value of the securities issued them resulting from increased assets. It follows, therefore, that the arguments of the petitioners based upon an alleged increase of assets are directed to matters which this Court has held lie within the province of the Commission.

(b) The Commission's permissible total capitalization of $75,000,000 does not afford a basis for determining a balance sheet solvency.

A fundamental error in the solvency argument of the petitioners lies in their use of the figure of $75,000,000 as a starting point in setting up a balance sheet of assets and liabilities. The Commission's valuation in the form of a permissible capitalization was based not upon the value of the Debtor's various assets as of any specific date, but rather upon an overall valuation for reorganization pur-

poses, which was arrived at after consideration of "all the data of record" including "traffic and earnings to the latest available date" and "also future prospects of traffic and earnings" (R. 3741, 3774-75). Thus this valuation takes into consideration the prospect of large wartime earnings and the increase in the current asset position of the Debtor, which the Commission was aware would ensue. The war earnings for rail carriers were well known to the Commission by March 9, 1942, when it filed its Supplemental Report, as shown by its pertinent references thereto in its Annual Report for 1941, pp. 1-2, and the Commission took these factors into account in making its determination of a permissible capitalization. The permissible capitalization fixed by the Commission rested upon its informed judgment, taking into consideration estimated improved current asset position and earning power. This capitalization cannot be considered as an exact valuation of assets at any specific date.

This Court has recognized that earning power is the primary criterion in determining capitalization for reorganization purposes rather than a balance sheet tabulation of assets and liabilities (*Milwaukee & Western Pacific* cases, *supra*). Whether or not junior securities are "without value" must depend primarily on earning power as this Court ruled in the *Milwaukee* case 318 U. S. p. 539:

> "* * * it [was not] necessary for the Commission to make a precise finding as to the value of the road in order to eliminate the old stock from the plan. A finding as to the precise extent of the deficiency is not material or germane to the finding of 'no value' prescribed by § 77 (e). * * * The basic question in a valuation for reorganization purposes is how much the enterprise in all probability can earn."

The entire solvency argument of petitioners is based upon their assumption that the Commission made a finding of "the precise extent of the deficiency" when it fixed the new

capitalization. But the Commission only made an overall valuation for reorganization purposes taking into consideration the prospective earnings (R. 3741, 3774-75) and other factors to which petitioners point as changed conditions necessitating amendment of the plan. Thus it is inaccurate to use the Commission's permissible capitalization as a starting point for a series of calculations intended to show the Debtor's present solvency through accumulation of assets sufficient to make up the supposed deficiency. As this Court stated in *Insurance Group Committee et al.* v. *The Denver and Rio Grande Western Railroad Company et al.* (15 U. S. Law Week, p. 4192, Feb. 3, 1947):

> "When the Interstate Commerce Commission finds the value of a railroad system by any means, the correctness of the result cannot be mathematically proved or disproved. The difficulties of appraisal are multiplied by the necessity of looking into the future to estimate earnings. Earnings estimates are made with allowance for changing economic conditions."

(c) No changed conditions have resulted from the cash distributions since the plan's effective date warranting review by this Court.

Under the terms of the plan, the District Court may direct that cash distributions made to senior creditors after the effective date shall be applied to the reduction in part of their claims. Yet, even if the court so applies whatever amount of the cash distributed since January 1, 1942, may be necessary to reduce or eliminate the unpaid interest claims of senior creditors and the amount of common stock is increased as a result of payment of the Railroad Credit Corporation loan, as provided in the plan, $1,584,709 of creditors' claims will receive no treatment under the plan:

Total permissible capitalization		$75,000,000
Deduct*: Equipment Trust Obligations paid off....	216,000	
Texarkana Union Station certificates paid off	315,000	
Interest Paid prior to effective date Funded Under Plan	400,000	
	931,000	931,000
		74,069,000
First Mortgage 4s	20,000,000	
Grays Point Terminal 5s	500,000	
Shreveport Bridge 5s	450,000	
Second Mortgage 5s	3,042,500	
First Terminal 5s	8,063,000	
General and Refunding 5s.....	#39,557,500	
Stephenville 5s	** 2,843,294	
Central Arkansas 5s	** 1,197,435	
		75,653,709
		(d) 1,584,709

If $1,584,709 of creditor claims are still unprovided for under the plan, there have plainly been no changed conditions resulting from cash distributions which warrant review of the plan by this Court.

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* No provision is made in the plan for reallocation of these amounts after payment of these obligations.

** Includes unpaid interest to 1/1/42 and after deducting salvage money that has been distributed.

Including Refunding Bonds pledged because Commission's plan treats such bonds as reduced to possession and accords holders of pledged bonds same treatment as public holders of Refunding Bonds.

(d) Deficiency. Even if securities released by payment of Equipment Trust Certificates, Texarkana Union Station Certificates and interest prior to January 1, 1942 are reallocated there would still remain unsatisfied claims of over $600,000.

The fact that the amount by which the creditors fail of complete satisfaction in face amount of new securities is now comparatively small, is of no consequence. Even if each creditor could now receive the full face amount of his claim in an equal face amount of new securities, it by no means follows that he has been made whole or that such a drastic unforeseen change in conditions has occurred necessitating a return of the plan to the Commission. This Court's recent ruling in *Insurance Group Committee et al.* v. *The Denver and Rio Grande Western Railroad et al.*, 15 U. S. Law Week 4189, p. 4191 places the burden upon the petitioners to show that the new securities over-compensate the creditors for their sacrifices in order to establish changed conditions invalidating a plan:

> "The Commission made no finding that the cash value of the securities allocated to the senior creditors paid them in full. To justify the change of position of creditors from fully secured to partially secured creditors were given opportunities to participate in profits through common stock ownership with a chance at larger earnings than the Commission's forecast anticipated. We held the priority rule was satisfied by this type of allocation. This was explained by our decision on the last review. Slip opinion, *supra*, p. 15. The debtor has made no allegation, either in this effort for re-examination or before, that the existing cash value of the securities allotted any creditor has ever aggregated the amount of the creditor's claim against the debtor. We think the absence of such an allegation, of itself, demonstrates that the plan is not, because of excessive interest, unfair to the debtor or those for whom it is allowed to appear.
>
> Until it can be contended with some show of reasonableness that the creditors senior to the creditors and stockholders whom the debtor represents here have received more in value than the face of their claims, the debtor's insistence on a re-examination of the plan is without substantial support. See *Northern Pacific Ry. Co.* v. *Boyd*, 228 U. S. 482; *Group of Investors* v. *Milwaukee R. Co.*, 318 U. S. 523, 541."

These petitioners have made no allegation and offer no proof to show that the creditors provided for under the plan have received more in value than the face of their claims. There is, then, no warrant for a review of the plan by this Court or a reconsideration of the plan by the Commission.

As a matter of record, the cash distributed to the creditors has not materially aided the Debtor in so far as its need for reorganization is concerned. As shown by the Debtor's balance sheet as of October 31, 1946, Appendix B to Southern Pacific's petition, it is still unable to meet its matured and maturing debts. The Debtor's matured principal obligations are $25,064,394. In addition the Debtor is obligated in the principal sum of $17,882,250 to Southern Pacific, which sum is now due. Its matured unpaid interest obligations are $3,247,284, excluding $1,443,540 interest in default on Southern Pacific's claim. There is the further obligation to pay current interest on the Debtor's first mortgage bonds and its equipment obligations. The Debtor has available to meet its matured and maturing debts, cash and temporary cash investments of $22,989,923 and total current assets of $32,545,847. Total current liabilities amount to $10,455,343, leaving $22,090,504 net current assets to meet matured and maturing obligations of $28,311,678 excluding Southern Pacific's matured claim of $19,325,790, principal and interest. If this sum be included, the Debtor's matured obligations are $47,637,468. It cannot be said, then, that the improved cash position of the Debtor and its debt retirement has placed it in any position to fully meet its matured or maturing obligations. It is, therefore, a proper subject for reorganization and the fundamental consideration under such circumstances in the formulation of a reorganization plan is the Debtor's prospective earning power. The Commission has found that the Debtor's normal earning power is insufficient to warrant a capitalization which permits participation by the equity or even full compensation of the creditors. As we point out below, petitioners have completely failed to present substantial evidence which would justify a finding that the Commission's conclusion in this respect was in error.

Even were the Debtor able and required to repay its interest arrears only and be relieved of its obligation to pay its matured principal debts, the problem for reorganization purposes would still remain its ability to meet its obligations as they mature. The obligations which Debtor would have to meet in fixed charges on its existing debt under its present capital structure would amount to $3,008,634 annually as shown by the Debtor's annual report for 1945. On the basis of the property's historical earnings record and all other factors the Commission has found that the Debtor has been and will be unable to meet such heavy fixed charges apart from its maturing principal obligations. The petitioners offer no reliable evidence to establish clear error in this determination.

Petitioners Have Made No Valid Showing Of Changed Conditions With Respect To The Debtor's Earning Power

The petitioners' second charge of inequity resulting from changed conditions is founded upon an alleged error in judgment on the part of the Commission in its determination of the prospective earning power of the Debtor. However, the only evidence cited in support of this claim is the 10 months earning statement of the Debtor for 1946, statistics showing an increase of population in the southwest territory, and a theoretical industrial expansion in that area. On these tenuous factors alone petitioners contend that this Court should set aside the considered judgment of the Commission as to the Debtor's normal earning power based upon a review of all relevant data together with its vast experience and familiarity with such matters. This inadequate record, consisting primarily of hopeful predictions by petitioners, presents no valid reason for this Court to review the determination of the Commission based upon its expert judgment. The allegations relied upon here with respect to the Debtor's earnings and earning power were presented to the Circuit Court as recently as October 22, 1946, when that Court denied petitions for rehearing. The Circuit

Court, sitting in and fully familiar with the alleged industrial and population expansion in the territory served by the Debtor, found nothing in the petitioners' allegations warranting a change in the Commission's plan. As recently as June 10, 1946, this Court considered and rejected almost identical arguments in the *Denver* proceeding.* On the basis of the proof offered in this proceeding they must likewise be rejected.

The petitioners rely almost entirely upon the ten months earning statement of the Debtor to contradict the Commission's determination as to the Debtor's prospective earning power. However, the figures themselves, while apparently favorable, may not be relied upon implicitly unless there is available the underlying data from which the result is derived. It is impossible to tell what non-recurrent income is contained in the ten months statement or to what extent tax carry back credits or inadequate maintenance provisions are responsible for the favorable statement. Furthermore from other aspects the Debtor's earnings picture has not been as optimistic. The Cotton Belt reported gross revenues for the full year of 1946 of $46.6 million representing a decline of 28% from 1945.** This is a substantially larger decline than that recorded by St. Louis-San Francisco, which showed a drop of only 17%, or by Missouri-Pacific which showed a decline of but 20%, both of which railroads are competitors of the Debtor. Class I railroads in general showed a decline of about 15%. The substantial decline in the Debtor's earnings may be attributed to the phenomenal rate at which the company's traffic increased during war years, since the Debtor showed one of the greatest percentages of increase of traffic among Class

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* This ruling was reaffirmed February 3, 1947. *Insurance Group Committee et al.* v. *The Denver and Rio Grande Western Railroad et al.*, 15 U. S. Law Week p. 4190.

** The source of the statistics cited herein is Moody's Railroads Service.

I railroads in the country for the war years. The peak traffic year of 1944 was for the Debtor 386% above its 1935-39 average as compared with 281% for the Missouri-Pacific, 270% for the St. Louis-San Francisco and 246% for Class I railroads generally. An important factor to bear in mind in reviewing the Debtor's war time earnings record is that during this period the Debtor's traffic "received from connecting lines" increased to 68% of its total traffic as compared with approximately 52% for years just prior to the war. There is plainly no certainty that the Debtor will continue to receive the very substantial increase in revenue from this form of traffic. Viewed in this light it would be wholly unsound to question the expert judgment of the Commission as to the Debtor's normal earning power merely on the strength of a ten months earning statement for 1946. Respondents submit that the petitioners have made no adequate showing to warrant review by this Court of the determinations of the three tribunals which have passed upon the question.

POINT II

The special charges of petitioner Meyer with respect to Southern Pacific's alleged illegal control of the Debtor present no questions for review by this Court.

Petitioner Meyer has renewed in his application to this Court the arguments he has made throughout this proceeding before the Commission (and subsequently before the District Court and Circuit Court of Appeals) of injurious control of the Debtor by Southern Pacific and other railroads. Principally, his contentions are that an alleged diversion of traffic from the Debtor and failure to solicit traffic preferentially distorted the Debtor's earnings record and, therefore, rendered the Commission's judgment of its prospective earning power erroneous. As a corollary to this

charge petitioner Meyer maintains that Southern Pacific's claim against the Debtor should be subordinated because of its breach of fiduciary duty to the Debtor. Nothing would be gained by a detailed review of the evidence before the Commission (or that introduced before the District Court) upon which the Commission rested its finding that Meyer's charges were without merit, which finding the District Court and Circuit Court have affirmed. Respondents believe it sufficient to point out that under the applicable decisions the charges of petitioner Meyer are not a proper subject for consideration by this Court.

In *Rochester Telephone Corp.* v. *U. S.*, 307 U. S. 125, this Court made the following statement of the basic rule of administrative law:

> "So long as there is warrant in the record for the judgment of the expert body it must stand. * * * 'The judicial function is exhausted when there is found to be a rational basis for the conclusions approved by the administrative body.' *Mississippi Valley Barge Line Co.* v. *United States*, 292 U. S. 282, 286-287; *Swayne & Hoyt, Ltd.* v. *United States*, 300 U. S. 297, 303, et seq."
>
> (Quoted with approval in *I. C. C.* v. *Jersey City*, 322 U. S., page 513).

A like rule has been laid down in connection with railroad reorganization proceedings under Section 77 where the scope of judicial review of Commission findings upon certain matters committed to its exclusive jurisdiction was defined as limited to ascertaining the existence of material evidence supporting the Commission's ruling and the observance of legal standards. *Western Pacific* case, *supra*, 318 U. S. p. 473.

It is well settled that the control of one carrier by another is a matter committed to the exclusive jurisdiction of the Interstate Commerce Commission (*New York Central Securities Co.* v. *U. S.*, 287 U. S. 12, p. 26). The Commission

has given approval to the control of the Debtor by Southern Pacific (*St. Louis S. W. Ry. Control,* 180 I. C. C. 175). Under the doctrine of the foregoing cases, therefore, it must follow that the propriety of the exercise of such control is a matter also committed to the exclusive jurisdiction of the Commission. And if it is found that its determination with respect thereto rests upon a sufficient record, compiled after opportunity for hearing has been given, the area of permissible judicial review has been covered.

Plainly, the Commission's rejection of the charges of improper control in this case is founded upon an ample record with full opportunity to be heard. Petitioner Meyer introduced considerable evidence on the subject at the initial Commission hearing in March and April, 1937 (R. 168-212). From May 5th through May 27th and from September 18th through 30th, 1939, the Commission held hearings solely to hear evidence in connection with the Meyer charges. The record compiled on this matter alone exceeded 2,500 pages as well as hundreds of exhibits (R. 529-3055). That the Commission painstakingly reviewed and weighed this evidence is shown by its first report which, for the most part, is devoted to a discussion of the Meyer charges (R. 3547-3678). Meyer's objections to the Commission's findings in that report were considered and again rejected by the Commission in its supplemental report (R. 3742-3752). When the plan was certified to the District Court Mr. Meyer was permitted to adduce a formidable amount of additional evidence in support of his charges (R. 4157-4199, 4202-4209, 4304-5166). Both the District Court and the Circuit Court of Appeals reviewed this vast record, found it more than adequate and concluded that no evidence had been presented demonstrating palpable error in the Commission's findings. On the basis of this ample record and opportunity to be heard respondents believe that this Court's settled decisions preclude a review of the petitioner's special charges. The issues raised by Mr. Meyer "are matters requiring study by experts on railroad affairs, involving as they do, expert analysis of traffic movements, freight loadings, financial

statements and other data peculiarly within the comprehension of the I. C. C. . . . " (District Court opinion, 53 F. Supp. p. 927). They are clearly, therefore, not proper matters for consideration by this Court.

CONCLUSION

The petitions for certiorari should be denied.

Dated: February 10, 1947.

Respectfully submitted,

EDWIN S. S. SUNDERLAND,
WILLIAM D. TUCKER JR.,
Attorneys for GUARANTY TRUST COMPANY OF NEW YORK,
as Trustee under the Debtors' First Terminal and Unifying Mortgage, Respondent

Nos. 879, 909 AND 936.

IN THE

Supreme Court of the United States

OCTOBER TERM, 1946.

SOUTHERN PACIFIC COMPANY, *Petitioner,*

v.

BERRYMAN HENWOOD, as Trustee of St. Louis Southwestern Railway Company Lines, *et al.*

WALTER E. MEYER, *Petitioner,*

v.

BERRYMAN HENWOOD, as Trustee of St. Louis Southwestern Railway Company Lines, *et al.*

ST. LOUIS SOUTHWESTERN RAILWAY COMPANY, *Petitioner,*

v.

BERRYMAN HENWOOD, as Trustee of St. Louis Southwestern Railway Company Lines, *et al.*

ON PETITIONS FOR WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE EIGHTH CIRCUIT.

BRIEF IN OPPOSITION

OF

THE CHASE NATIONAL BANK OF THE CITY OF NEW YORK AND MISSISSIPPI VALLEY TRUST COMPANY.

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February 22, 1947.

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ON PETITIONS FOR WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE EIGHTH CIRCUIT.

BRIEF IN OPPOSITION

OF

THE CHASE NATIONAL BANK OF THE CITY OF NEW YORK AND MISSISSIPPI VALLEY TRUST COMPANY.

Opinions Below.

The Report and Order of the Interstate Commerce Commission (herein called "Commission") of June 30, 1941 (R. 3495-3735) are reported in 249 I. C. C. 5, and its Supplemental Report and Order of March 9, 1942 (R. 3736-3820) are reported in 252 I. C. C. 325. The opinion of the District Court (R. 5183-5213) is reported in 53 F. Supp. 914. The opinion of the Circuit Court of Appeals (R. 5559-5683) is reported in 157 F. (2d) 337.

Jurisdiction.

The judgment of the Circuit Court of Appeals was entered August 26, 1946 (R. 5681-5683). Petitions for rehearing were denied October 22, 1946 (R. 5831). The petitions for writs of certiorari were filed, respectively, January 13, 1947 (No. 879), January 18, 1947 (No. 909), and January 21, 1947 (No. 936). The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

Principal Questions Presented.

(1) Whether the Circuit Court of Appeals erred in refusing to remand the proceedings to the Commission because of the Debtor's substantial earnings subsequent to the Commission's formulation of the Plan, as a result of which, it is alleged, the Debtor is no longer "insolvent"? (Nos. 879, 909, and 936.)

(2) Whether the Circuit Court of Appeals erred in refusing to remand the proceedings to the Commission because of events transpiring subsequent to the formulation of the

Plan, as a result of which, it is alleged, Debtor's earning power is now substantially greater than it was at the time the Commission formulated the Plan? (Nos. 879, 909, and 936.)

(3) Whether the Circuit Court of Appeals erred in holding that there was substantial evidence to sustain the Commission's findings, affirmed by the District Court,—

(a) that the Debtor's earnings were not impaired by reason of the breach of fiduciary or other obligations, or by violations of the anti-trust laws, on the part of Southern Pacific Company and others, and

(b) that the Southern Pacific Company has not been guilty of "wrongful, illegal and unconscionable" acts in respect of the Debtor? (No. 909.)

(4) Whether the Circuit Court of Appeals correctly held that the procedure followed by District Judge Moore upon the death of Judge Davis did not constitute an abuse of discretion? (No. 909.)

(5) Whether the Circuit Court of Appeals abused its discretion in denying the motion of Petitioner Meyer to remand the case to the Commission on the ground of alleged newly-discovered evidence? (No. 909.)

Statutes Involved.

These cases arise under Section 77 of the Bankruptcy Act, as amended (11 U. S. C. A. 205). Pertinent provisions of Section 77, particularly subdivision (c) thereof, are quoted in appendices to the Petitions.

Statement.

The Debtor filed its petition for reorganization under Section 77 of the Bankruptcy Act on December 12, 1935 (R. 24-27), and thereafter similar petitions were filed by its three subsidiaries (R. 57-76). Objections to Debtor's petition by Walter E. Meyer and others (R. 83-87) were overruled by the District Court (R. 87-91). On January 3, 1936, a Trustee was appointed (R. 93-96).

On December 7, 1936, Debtor filed a proposed plan of reorganization; and thereafter other plans were filed (R. 3515-3546). Hearings on all these plans were begun before the Commission on March 16, 1937, and concluded on April 24, 1937 (R. 96-216). A substantial portion of the testimony related to various charges against Southern Pacific Company by Walter E. Meyer (R. 168-212).

In April, 1937, Walter E. Meyer filed with the Commission a voluminous petition for an investigation of his said charges (R. 339-351), which was followed on June 19, 1937, by an amended and supplemental petition for investigation and for reopening the proceedings (R. 357-467). These petitions were denied by the Commission on July 12, 1937 (R. 479-480).

On February 7, 1938, Examiner Walsh of the Commission issued a Proposed Report containing a plan which varied from the plans theretofore submitted (R. 255-339),[1] in which he rejected Mr. Meyer's contentions (R. 306-314).

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[1] The Examiner proposed a capitalization variable in amount depending on whether the claims of the holders of the Debtor's First Terminal and Unifying Bonds were held to be payable in guilders. These claims were ultimately held by the Supreme Court not to be payable in guilders. *Guaranty Trust Co.* v. *Henwood*, 307 U. S. 247 (1939).

Exceptions to this Proposed Report were argued orally before the Commission on May 16, 1938.

On January 10, 1939, in response to a further petition filed by Walter E. Meyer in April, 1938 (R. 480) and a memorandum filed by him in November, 1938 (R. 480-500), the Commission reopened the proceedings for the purpose of receiving further evidence relating to charges made by Meyer with respect to the effect upon the Debtor's earnings and assets of control by Southern Pacific (R. 500-501). Thereafter, hearings were held *for this sole purpose* from May 5, 1939, to May 27, 1939, and from September 18, 1939, to September 30, 1939 (R. 529). At these hearings a vast amount of evidence, including hundreds of exhibits, was introduced (R. 529-2680, 2681-3055).

On June 30, 1941, the Commission issued its initial Report and Order setting forth its Plan for the Debtor (R. 3495-3735; 249 I. C. C. 5). In said Report, of which 131 pages are devoted to an elaborate consideration of the Meyer charges (R. 3547-3678), the Commission, so far as the present petitions are concerned, found and determined—upon "a consideration of the entire record, including the elements of value referred to, the earnings and prospective earnings" (R. 3700)—

> (1) that the "fixed-interest charges immediately following reorganization should be about $1,500,000 a year" (R. 3691); that "the new capitalization should not exceed approximately $75,000,000, of which not more than one-half should be in the form of debt, nor more than one-fourth in the form of preferred stock, and the remainder in common stock" (R. 3692); that "debt claims totaling $8,304,118 can receive no recognition within the limits of capitalization approved" (R. 3700); that "the equities of the holders of the stock of the debtor have no value"

(R. 3700); and that therefore the stockholders could recieve no recognition in the reorganization; and

(2) that the charges of Walter E. Meyer against Southern Pacific were entirely without foundation (R. 3547-3678).

Thereafter petitions for modification of the Plan were filed. On March 9, 1942, the Commission issued its Supplemental Report and Order, which modified its original plan in certain relatively minor respects but which reaffirmed the same so far as the present petitions are concerned (R. 3736-3820; 252 I. C. C. 325). On March 23, 1942, the modified plan was certified to the District Court (R. 3494-3495).

From October 26, 1942, to November 5, 1942, hearings were held before the late Judge Davis upon objections to the Plan, at which additional evidence, including data as to recent earnings, was presented (R. 4051-5136). The great bulk of such additional evidence related to the charges made by Walter E. Meyer against Southern Pacific (R. 4157-4199, 4202-4209, 4304-5136). The parties stipulated that the entire record before the Commission and "every record that has been made in this case from its inception" should be deemed in evidence before the District Court (R. 4057).

Prior to the filing of briefs in support of the Plan and objections thereto, Judge Davis died. The case was then referred to Judge Moore (R. 5138), who, after a conference with counsel, including Mr. Meyer, on April 23, 1943, entered an order directing a reargument on May 31, 1943, upon the case as submitted before Judge Davis, with all parties having the right to apply for leave to present additional testimony (R. 5181-5183).

In the meantime, on March 15, 1943, the Supreme Court handed down its opinions in the *Western Pacific* (318 U. S. 448) and *Milwaukee* (318 U. S. 523) cases. Thereafter the

principal contentions now made by Petitioners were argued orally and on written briefs before Judge Moore. At this hearing *neither Mr. Meyer nor any other party sought leave to present additional evidence.* On February 8, 1944, the District Court filed an opinion and entered an order in which it approved the Plan (R. 5183-5212; *In re St. Louis Southwestern Ry. Co.,* 53 F. Supp. 914).

Upon appeals from said order by Petitioners and others (which were argued in April, 1945), all the principal contentions now made by Petitioners were, in essence, argued orally and on written briefs. On August 26, 1946, the Circuit Court of Appeals (which apparently held up its opinion until the coming down of the decision of this Court in the *Denver* case) affirmed the order of the District Court except in a minor respect not here relevant (R. 5559-5683; *St. Louis Southwestern Ry. Co.* v. *Henwood,* 157 F. (2d) 337). Thereafter petitions for rehearing were denied (R. 5831).

ARGUMENT.

PART I.

The contention that the Plan has become unfair because of changed conditions.

1. To the extent to which it has not already been foreclosed by the decisions of the courts below, Petitioners' contention is one which should be, and can be, presented in the first instance to the District Court; and there will still be opportunity for final review by this Court.

Petitioners' complaints stem from the Commission's finding (R. 3692, 3700), affirmed by both courts below (R. 5211-5212, 5653-5671), that the value of the Debtor's properties for purposes of the plan is $75,000,000. Because this

sum did not provide sufficient capitalization to take care of all creditor claims, the Commission found that the equity of the stockholders was without value (R. 3700), and both courts below have affirmed this finding (R. 5211-5212, 5653-5671).

Petitioners do not assert that the decision of the Commission was erroneous when made, *i.e.*, on the basis of the evidence then before the Commission.[2] They do not even assert that the decision of the District Court, affirming the finding of the Commission, was erroneous when made. Their basic contention here is that since the decisions of the Commission and the District Court—

> (1) the assets of the Debtor have increased so substantially, as the result of large earnings, that the Debtor is now "solvent," and
>
> (2) the earning power of the Debtor has increased so substantially as to bring about a fundamental change in the basic factor on which the Commission predicated its finding of value,

so that the Plan may no longer be regarded as "fair and equitable".

Respondents question whether there exists any "changed conditions" which clearly were not in contemplation of the Commission. But whether or not there has been such a change is not an issue which this Court should be asked to decide on the basis of conflicting and unverified assertions made in briefs—at least at this stage in the

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[2] The Debtor expressly disclaims any challenge of the Commission's findings (No. 936, p. 25).

The Petitioner Meyer, of course, challenges the Commission's findings to the extent that it did not accept the charges made by him against Southern Pacific and others.

proceedings. This is an issue of fact which (to the extent to which it has not been foreclosed by the decisions of the two courts below)[3] should be presented to the District Court, which can receive evidence *pro* and *con; and there will be at least two opportunities for Petitioners to raise this issue in the District Court before the Plan can be confirmed.*

In the case at bar, unlike the *Denver* case decided by this Court in June, 1946, and again in February, 1947, the Plan has not yet been submitted to the creditors for a vote. Under Section 77(e), the next step in the instant case (if the petitions for certiorari be denied and if the District Court does not direct different action) is for the Commission to submit the Plan to the creditors for a vote thereon. When such vote has been taken, the Plan must come again before the District Court to be confirmed; and at that time (as made clear by this Court in the *Denver* case) Petitioners can raise the contentions which they are here making. At that time (if any class of creditors have rejected the Plan) Petitioners will be in a position to support such contentions by evidence; and parties wishing to oppose the same will be able to offer contrary evidence.

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[3] In *Insurance Group Committee, et al.* v. *The Denver and Rio Grande Western Railroad Company, et al.*, No. 690, October Term, 1946, decided February 3, 1947, this Court said:

> "* * * we ruled in our decision of June 10, 1946, * * * that in this reorganization no changed circumstances, up to that date, presented to us by the debtor or other respondents in that review justified a re-examination of the plan as confirmed. This ruling was binding upon the District Court and the Circuit Court of Appeals as to changed circumstances arising after the order of confirmation and prior to our decision. When matters are decided by an appellate court, its rulings, unless reversed by it or a superior court, bind the lower court. * * *"

Even before the Plan is submitted for a vote, the District Court will be in a position (after the disposition of the pending petitions for certiorari) to remand the Plan to the Commission *not for submission to the creditors, but for a re-examination of the question of the fairness of the Plan in the light of changed conditions.* As a matter of fact, a petition to this end is now pending in the District Court and will undoubtedly be brought on for hearing as soon as the District Court has recovered jurisdiction over the Plan.[4]

When the Commission approved the Plan, it necessarily undertook to forecast the Debtor's *future* earnings. As stated in *Insurance Group Committee, et al.* v. *The Denver and Rio Grande Western Railroad Company, et al.*, No. 690, October Term, 1946, decided February 3, 1947, earnings estimates by the Commission "are made with allowance for changing economic conditions." If the Commission's forecast was made on sound principles (and Petitioners do not here assert the contrary), it must be accepted as valid, under the *Western Pacific* and *Milwaukee* decisions, unless and until it can be demonstrated that there has been a change of conditions which clearly was not envisaged by the Commission. As late as October, 1946, when the petitions for rehearing were denied, the Circuit Court of Appeals held that there had been no such change. Conceivably, notwithstanding the finding, it may be shown that, in the light of changes since October, 1946, there have been material changes not contemplated by the Commission; but, at this stage of the proceedings, the place for such a showing is the District Court.

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[4] Late in December, 1946, one Carl Rosenberger, owner of certain bonds and stocks of the Debtor, filed a motion in the District Court asking that the Plan be remanded to the Commission because of "changed conditions." The hearing on said motion has been set for March 28, 1947.

When, many months hence, the Plan comes before the District Court for confirmation, Petitioners will be able to raise the point of "changed conditions". If their contentions are rejected they may appeal to the Circuit Court of Appeals; and if unsuccessful there, they will still have recourse to the Court upon certiorari.

If, in the case at bar, this Court should now undertake to decide whether there have been "unanticipated, large earnings" during the period between the Commission's formulation of the Plan and the time of this Court's decision, and should decide that there had been none, grave injustice might be done, and no real progress would have been made toward the consummation of a Plan. This Court's decision would have covered *only a part* of the period with respect to which an objector to the Plan could introduce evidence (as to changed conditions) when the Plan comes before the District Court for confirmation; the position of the objectors to the Plan would be weakened to a substantial but indeterminate extent; and those who supported the Plan would still have no assurance that the Plan would eventually be confirmed.

2. The applicable principles have been fully stated by this Court in recent decisions.

In every Section 77 proceeding in which the plan was formulated by the Commission prior to, or during the early stages of, the recent war, contentions have been advanced which are, in all substantial respects, identical with those here asserted, *i.e.*, that the plan has become inapplicable because of "changed conditions" resulting from "unanticipated, large earnings." Three such cases have been reviewed by this Court, one quite recently. In each such case this Court, while recognizing the power of a District Court to remand the plan to the Commission because of changed

conditions (and also the power of an appellate court under certain circumstances to remand the plan to the Commission for the same reason), has held that the objectors had failed to sustain the burden of showing that there had been a change of conditions which could not fairly be said to have been in the contemplation of the Commission when the plan was formulated.

In *Ecker* v. *Western Pacific R. Corp.*, 318 U. S. 448 (1943), the Court said (pp. 507, 508, 509):

> "• • • Respondents ask us to take into consideration the changed conditions since the Commission acted. • • •
>
> "In the interest of advancing the solution of as many problems in reorganization as possible, we have deliberated upon the effect to be given these unexpectedly large earnings. There are factors in these increased incomes which obviously affect their weight as evidence of continued capacity to produce earnings available for dividends. • • •
>
> • • • • • •
>
> "• • • The Commission's forecast was made with knowledge and not in disregard of past fluctuations of income, in war and in peace. On the showing as to changed conditions made before the District Court, there was no basis for a disapproval of the Commission plan as unfair to the junior equities. The further evidence of increased earnings, placed in the record by the stipulations, does not lead us to reject the Commission's plan."

Dealing with the same issue, this Court, in *Group of Investors* v. *Milwaukee R. Co.*, 318 U. S. 523 (1943), said (pp. 542, 543, 544):

> "The question of the increase in earnings since the Commission approved the plan raises of course different issues. As we have indicated in the *Western*

Pacific case, the power of the District Court to receive additional evidence may aid it in determining whether changed circumstances require that the plan be referred back to the Commission for reconsideration. * * *

"We agree with the Circuit Court of Appeals that no sufficient showing of changed circumstances has been made which requires the District Court to return the plan to the Commission for reconsideration. * * * In view of these considerations, we cannot say that the junior interests have carried the burden which they properly have of showing that subsequent events make necessary a rejection of the Commission's plan."

Still later, in *Reconstruction Finance Corp.* v. *Denver & R. G. W. R. Co.*, decided June 10, 1946, this Court said (66 S. Ct. 1282, 1291, 1296):

"* * * Changes in economic conditions cannot affect the powers of the reorganization agencies even though such changes may require a reexamination into the present fairness of the former exercise of those powers.

* * * * * *

"* * * Assuming that the courts, as courts with equity powers in a bankruptcy matter, might set aside a plan, fair and equitable when adopted by the Commission, merely on account of subsequent changes in economic conditions of the region or the nation, it should not be done when the changes are of the kind that were envisaged and considered by the Commission in its deliberations upon or explanation of the plan."

The matter was even more recently before this Court in *Insurance Group Committee, et al.* v. *The Denver and*

Rio Grande Western Railroad Company, et al., No. 690, October Term, 1946, decided February 3, 1947. In that case the Court assumed, arguendo, "that both this Court upon appeal from an order of confirmation in bankruptcy, and the bankruptcy court itself, after its order of confirmation has been affirmed on review (11 U.S.C. § 205(f)), may take cognizance of subsequent changes in conditions and order a plan re-examined by the Interstate Commerce Commission"; and then, after outlining facts alleged to show "changed conditions" of substantially the same general character as those alleged in the case at bar, held "that the debtor has failed to allege the existence of changed conditions since our decision of June 10, 1946, of a kind not 'envisaged and considered by the Commission in its deliberations upon or explanations of the plan.'" The Court further stated:

> "Much of what we have written is directed at the suggestion that there should be a plenary re-examination of reorganization proposals for the Denver & Rio Grande. As to that suggestion, we are of the opinion that the record affirmatively shows a proper basis for the valuation and allocation of securities by the Commission, * * * and that the record fails to show any sound basis for a re-examination on account of changed circumstances between May, 1941, and June 10, 1946.
>
> "So far as the period since June 10, 1946, is concerned, there is no basis in this record or in anything judicially known to us for a conclusion that there has been a significant change in interest rates, earnings available for interest or traffic. Nor do we see that the action of Congress in passing S. 1253, on July 31, 1946, should persuade us to require a stay to await further enactments that might affect this reorganiza-

> tion. It was vetoed. * * * We must continue to act under the now existing law.* * *"

The Circuit Court of Appeals in the case at bar had all except the last of these decisions before it when it reached its decision. In fact, there is reason to believe that the Court held up its decision for several months awaiting the June 10, 1946, decision in the *Denver* case. The only issue thus presented is whether, on the particular facts of this case, the court below correctly applied the applicable principles so recently and fully stated by this Court. We respectfully submit that this does not raise an issue which should be reviewed by this Court.

3. Petitioners have misconceived the basis upon which the relief they seek should be predicated.

Petitioners have consumed much space in endeavoring to show that, because of decrease in indebtedness and increase in current assets, the Debtor is now "solvent". The present proceedings, however, were not instituted because Debtor was "insolvent", but because it was "unable to meet its debts as they matured" (R. 26). This latter allegation alone was all that was necessary to give the District Court jurisdiction (11 U. S. C. A., §205 (a)). Plainly, therefore, in determining whether the stockholders have been improperly excluded from the Plan, the test is not whether the Debtor is "insolvent", but whether the stockholders' equity possesses a real value; and the answer to this question, in an appellate court, must always be in the negative unless the stockholders can demonstrate affirmatively that the Plan not only fully satisfies the admittedly prior claims of the creditors, but *actually overpays the creditors.*

Thus, in *Insurance Group Committee, et al.* v. *The Denver and Rio Grande Western Railroad Company, et al.*, No. 690, October Term, 1946, decided February 3, 1947, this Court said:

> "The Commission made no finding that the cash value of the securities allocated to the senior creditors paid them in full. To justify the change of position of creditors from fully secured to partially secured, creditors were given opportunities to participate in profits through common stock ownership with a chance at larger earnings than the Commission's forecast anticipated. * * * The debtor has made no allegation, either in this effort for re-examination or before, that the existing cash value of the securities allotted any creditor has ever aggregated the amount of the creditor's claim against the debtor. We think the absence of such an allegation, of itself, demonstrates that the plan is not, because of excessive interest, unfair to the debtor or those for whom it is allowed to appear.
>
> "Until it can be contended with some show of reasonableness that the creditors senior to the creditors and stockholders whom the debtor represents here have received more in value than the face of their claims, *the debtor's insistence on a re-examination of the plan is without substantial support.* * * *" (Italics supplied.)

In the case at bar Petitioners have not even alleged, let alone undertaken to show, that the creditors whose claims are treated in the Plan have been, in effect, overpaid. In this connection, it may be pointed out that in spite of Debtor's admittedly high earnings, its First Terminal and Unifying Bonds (having a total claim for principal and interest of over 102) are now selling on the New York Stock

Exchange at about 80, and its General and Refunding Bonds (having a total claim of approximately 122) are selling at about 88.

4. The validity of Petitioners' basic assumption has not been established.

Underlying Petitioners' contentions is the assumption that since the Commission formulated the Plan, Debtor's assets have increased to a point where it is now "solvent." Without undertaking to discuss the question whether Debtor is or is not now "solvent", we point out that Petitioners' assumption is predicated upon a misapprehension of the bases on which the Commission arrived at a total valuation of $75,000,000.

Thus, Southern Pacific argues: When the Commission fixed a valuation of $75,000,000, there was a "deficit" of $8,304,118, *i.e.*, the debt claims exceeded $75,000,000 by only $8,304,118;[5] comparing Debtor's August 31, 1941, balance sheet (which, Southern Pacific asserts, "may be regarded as forming the basis for the Commission's values in its Supplemental Report") with its balance sheet for October 31, 1946, there has been an increase in current assets and a decrease in debt aggregating $27,119,075, so that Debtor is now "solvent" by a margin of $18,800,000, or, if the debt is computed on the basis of the pledged bonds held by certain noteholders rather than on the basis of the notes held by such noteholders (as, of course, it must be, since under the Plan the noteholders are treated as if they were the outright owners of the pledged bonds held by them),

[5] If the debt claims were computed on the basis of the pledged Bonds held by three noteholders (who, under the Plan, are treated as the outright owners of the pledged Bonds), the "deficiency" would have been over $20,000,000.

Debtor is now "solvent" by a margin of $6,800,000 (No. 879, pp. 8, 28, 29).

A basic flaw in this argument is the assumption that the Commission's valuation of $75,000,000 *did not take into account future prospects of large earnings which, as the District Court put it* (R. 5208), *was "apparent from the circumstances prevailing."* This assumption is plainly ill-founded.

In its initial Report, the Commission stated that it fixed the new capitalization of $75,000,000 on the basis of "all the data of record on property valuation and past and *prospective* earnings" (R. 3692). In its Supplemental Report it pointed out that it had considered "all the data of record" including "traffic and earnings to the latest available date" and "also *future prospects* of traffic and earnings"; and that it arrived at the sum of $75,000,000 upon "a consideration of the earning power of the property, past, present and *prospective,* and all other relevant facts" (R. 3741, 3774-3775).

It is thus clear that the Commission undertook to fix an over-all value for the Debtor's properties, and that in fixing such over-all valuation the Commission gave greatest weight to earning power, including "traffic and earnings to the latest available date" and "also *future prospects* of traffic and earnings."[6]

Since, therefore, in arriving at the $75,000,000 valuation the Commission took into account the prospective large earnings resulting from the war (*i.e.*, the very earnings which Petitioners now offer as a basis for suggesting that the Commission might change its mind if it were required to

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[6] The District Court, following the *Western Pacific* and *Milwaukee* cases, properly held that the Commission was not required to spell out in detail the precise method by which it arrived at the $75,000,000 valuation (R. 5206).

consider the matter again), Petitioners may not properly compare Debtor's current balance sheet with the balance sheet for August 31, 1941, or for any earlier date, and assume that any intervening increment in assets represents an increase in the valuation of the properties *over and above that fixed by the Commission.* To state it differently, the changes in net current assets or other assets since the date of the Commission's Supplemental Report may not represent an *increase* in the over-all value as found by the Commission, but merely a *realization* of the total value which the Commission reached on the basis of "future prospects of traffic and earnings" (R. 3741).

Impliedly recognizing this weakness in their argument, Petitioners seek to escape it by suggesting that, whereas in the *Denver* case the plan was not formulated by the Commission until June, 1943, in the case at bar the Commission's "last look" at the situation was in March, 1942, over a year earlier. This discrepancy in time would seem to be of little consequence. In the case at bar the European war had been under way for *nearly two years* at the time of the initial Report of June 30, 1941, and its effect was being sharply reflected in all railroad earnings. The Commission itself pointed out in said Report (R. 3691) that Debtor's earnings for the first four months of 1941 indicated that its income available for fixed charges for that entire year would be "substantially in excess of the Trustee's forecast of $4,142,000." At the time of the Supplemental Report of March 9, 1942, the United States had been at war for several months; and the Commission was fully aware that in 1941 Debtor had earnings available for fixed charges of $7,495,940.40, a figure which was substantially in excess of earnings for any year in Debtor's prior history (R. 2683, 5205) and not greatly less than Debtor's earnings for 1942,

1943, and 1944. Debtor's income available for fixed charges in 1941 was in excess of the comparable figure for 1945 (R. 5727), and, on the basis of income available for fixed charges of $6,803,389 for the first 11 months of 1946 (Trustee's Monthly Report dated January 13, 1947, filed in the District Court), was almost exactly identical with its probable earnings for 1946. Necessarily, therefore, this Court must assume that the Commission's valuation would have been *substantially less than $75,000,000* had it not been for the weight which the Commission said it gave to "prospective" earnings.

Obviously, therefore, the "solvency" of Debtor cannot be tested by adding to said sum of $75,000,000 the amount of the increase in Debtor's assets since the Commission's formulation of the Plan.

5. There is no conflict of decisions.

The Petitioner Southern Pacific Company asserts (No. 879, pp. 41-43) that the decision of the court below is in conflict with the recent decision of the District Court for the Northern District of Illinois in the *Rock Island* case, now pending on appeal, in which Judge Igoe refused to *confirm* the plan because of radical changes in the debtor's earnings and assets subsequent to the Commission's formulation of the plan (see, Appendix E, No. 879). In the *Rock Island* case, however, the plan had been voted on and was up before the District Court for *confirmation;* and the basic question before the District Court, as in the *Denver* case (66 S. Ct. 1282), was whether the refusal of certain classes of creditors to approve the Plan was "reasonably justified in the light of the respective rights and interests of those rejecting it and all the relevant facts." As pointed out above (pp. 9-11, *supra*), that stage has not been reached in the case at bar.

Moreover, apart from the fact, there is no conflict. Both decisions recognize the power of a court, under proper circumstances, to remand the Plan because of "changed conditions".

The Debtor asserts (No. 936, pp. 43-48) a conflict with the decision of the Second Circuit in the so-called *Equitable Building* case,—*Adelaide H. Knight et al.* v. *Wertheim & Co., et al.,* decided December 31, 1946 (see, Appendix D, No. 936). In that case, a proceeding under Chapter X of the Bankruptcy Act, the Circuit Court of Appeals held that the District Court had abused its discretion in refusing, prior to final consummation of the plan, to submit to the shareholders an offer to purchase the new company's shares at a price which, together with the bankrupt's liquid assets, *would have permitted paying off the creditors in full, both principal and interest.* In holding that the District Court had abused its discretion, the Court said, in effect, that "If the legally protected interests of any opposing parties are fully preserved," there is no "good reason to deny others any reasonable chance to protect their own interests * * *." The situation in the *Equitable* case is wholly unlike that in the case at bar, since here Petitioners do not even suggest that if the Plan is remanded to the Commission, the creditors will be paid off in full, both principal and interest.

PART II.

The special contentions of petitioner Walter E. Meyer (No. 909).

1. The Circuit Court of Appeals fully performed the required judicial review and correctly held that there was substantial evidence to sustain the Commission's finding, affirmed by the District Court, that the Debtor's earning power has not been impaired by breaches of fiduciary and other obligations by Southern Pacific and others.

Mr. Meyer's chief contention is that the Commission's findings as to valuation and capitalization were predicated upon an erroneous conception of Debtor's real earning power because it did not take into account various alleged breaches of fiduciary and other obligations by Southern Pacific which are said to have impaired Debtor's earnings and assets (No. 909, pp. 2, 19, 26). Thus, he alleges that after Southern Pacific acquired control of Debtor in April, 1932, it failed to obtain for Debtor large amounts of traffic which it should have obtained (No. 909, pp. 7-8); that it failed to carry out the Turney-Saunders agreement to solicit traffic preferentially for Debtor (No. 909, p. 8); and that it caused Debtor to solicit traffic contrary to its best interests (No. 909, pp. 8-9). He further contends that prior to Southern Pacific's acquiring control in 1932, Debtor had been under the illegal control of various competitive railroads, including Southern Pacific, as the result of which its assets had been wasted and earnings impaired (No. 909, pp. 3-6). He also contends that Southern Pacific's claim as a creditor and stockholder should be expunged, or at least subordinated, not only because of the matters above alleged, but because Southern Pacific prevented Debtor from enforcing causes of action under the anti-trust laws

against Kansas City Southern and others (No. 909, pp. 2, 26, 34-36). Finally he asserts that the Plan was formulated on inadequate data, that he was not afforded an adequate opportunity to present evidence of his charges, and that the Commission failed to make an independent investigation of his charges (No. 909, pp. 37-42).

A large amount of evidence purporting to sustain these charges was introduced by Mr. Meyer at the initial Commission hearings in March and April, 1937 (R. 168-212). Thereafter said charges were the subject of further hearings before the Commission, held solely for the purpose, from May 5 to May 27, and from September 18 to September 30, 1939, at which a vast amount of evidence, including hundreds of exhibits, was introduced (R. 529-3055). This evidence was exhaustively considered by the Commission in its initial Report, wherein (after discussing in detail *every allegation by Mr. Meyer*) it concluded that none of the charges was well-founded (R. 3547-3678).

After the Commission issued its initial Report of June 30, 1941, Mr. Meyer filed numerous objections thereto. The Commission carefully considered these objections in its Supplemental Report of March 9, 1942, and concluded that none of them was well-founded; and it reaffirmed its original determinations with respect to the Meyer charges (R. 3742-3752).

Thereafter, at the hearing before the District Court upon objections to the Plan, Mr. Meyer reiterated his charges against Southern Pacific, and introduced a large amount of additional evidence with respect thereto (R. 4157-4199, 4202-4209, 4304-5166).

Mr. Meyer asserts (No. 909, pp. 3, 19, 31-32) that the District Court did not review the Commission's findings and that the Circuit Court of Appeals did not make an

"adequate review." The record shows clearly, however, that the District Court carefully considered Mr. Meyer's charges specifically and in detail (R. 5197-5203) in its opinion of February 9, 1944, and concluded (R. 5202) that Mr. Meyer "has not convinced either this Court or the Commission that his charges are well-founded."[7] It further found (R. 5202):

> "* * * that ample opportunity has been afforded to Mr. Meyer by the Commission and by the Court to present evidence in support of his various allegations and objections, and that the time elapsed during the pendency of these proceedings has afforded ample time for him to fully prepare his case."

With respect to Mr. Meyer's contention that Southern Pacific's creditor claim should be expunged or subordinated, the District Court pointed out the additional facts that certain parties, but not Meyer, filed objections in the District Court to Southern Pacific's claim; that extended hearings on such objections were held before a Special Master who found in favor of Southern Pacific; that exceptions were taken to the Master's report which were overruled and the claim allowed; and that in view of Meyer's failure to avail himself of the chance to object to Southern Pacific's claim he may not be heard to make any objection (R. 5199).

Upon appeal the Circuit Court of Appeals dealt exhaustively and painstakingly with each of Mr. Meyer's charges, devoting 88 out of 117 pages of its opinion to these matters (R. 5564-5652).

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[7] As to the charge of derelictions by Southern Pacific prior to April, 1932, see R. 3637; as to alleged derelictions after April, 1932, including the alleged failure to carry out the Turney-Saunders agreement, see R. 3669-3670; as to the charge that Southern Pacific prevented the Debtor from asserting causes of action for violation of the anti-trust laws, see R. 3678; as to the charge that Mr. Meyer's contentions were not adequately investigated, see R. 3549-3676.

A review of the voluminous record shows, we submit, that rarely before have so many charges received such prolonged and careful attention by so many administrators and judges.

As stated by the District Court (R. 5203), the issues raised by Mr. Meyer "are matters requiring study by experts on railroad affairs, involving, as they do, expert analysis of traffic movements, freight loadings, financial statements and other data peculiarly within the comprehension of the I. C. C." In view of the finality which attaches to the Commission's findings of fact, and particularly findings as to valuation, capitalization and all other matters affecting the public interest, we submit that the affirmation of the Commission's emphatic rejection of Mr. Meyer's charges by both courts below is conclusive upon this Court. See, *U. S.* v. *Commercial Credit Co., Inc.*, 286 U. S. 63, 67 (1932); *Texas & N. O. Railroad Co.* v. *Ry. Clerks*, 281 U. S. 548, 558 (1930).

2. The Circuit Court of Appeals correctly held that the procedure followed by District Judge Moore upon the death of District Judge Davis did not constitute an abuse of discretion.

Mr. Meyer's contention that he was entitled to a "new trial" upon the death of Judge Davis is wholly ill-founded.

After the Commission certified the Plan to the District Court, hearings were held on objections thereto before the late Judge Davis (R. 4051 *et seq.*). At these hearings additional evidence was introduced, the bulk of which was presented by Mr. Meyer (R. 4157-4199, 4304-5136). During the hearings all parties presented their respective arguments except Debtor and Mr. Meyer, whose arguments were set down for hearing on December 18, 1943 (R. 4991). Before these arguments were had and briefs filed, Judge Davis

died. Thereafter the parties appeared before Judge Moore, to whom the case was assigned, to discuss the procedure to be followed. After an extended discussion (R. 5138-5180), Judge Moore entered an order, dated April 23, 1943, that the record on the Plan as certified by the Commission and the record theretofore made before the late Judge Davis be taken as submitted, that the Plan and the objections thereto and claims for equitable treatment be set down for oral argument on May 31, 1943, and that during or at the conclusion of said oral argument the Court *would entertain any motion respecting the taking of additional testimony or otherwise pertaining to the completion of the record on the Plan* (R. 5182). The District Court reserved the right to amend or modify the order in any manner consistent with Section 77 (R. 5183). On May 31, 1943, the parties appeared by counsel before Judge Moore and submitted their respective oral arguments. *Neither Mr. Meyer nor any other party made any request for leave to present additional evidence.*

Mr. Meyer contends (No. 909, pp. 47-50) that upon the death of Judge Davis he was entitled to a complete hearing *de novo*. The Circuit Court of Appeals held that the granting of a hearing *de novo* was a matter within the discretion of the District Court and that that court did not abuse its discretion in following the procedure above outlined (R. 5567-5569).

Whatever may be the applicable rule with respect to ordinary jury or non-jury trials, these respondents submit that none of the parties was entitled, as of right, to a hearing entirely *de novo* after the death of Judge Davis. Under the special statutory reorganization scheme of Section 77, by which the functions of the Commission and the District

Court are "brigaded,"[8] the great bulk of the evidence, of necessity, is presented in the first instance to the Commission; and this evidence necessarily comes before the District Court in the form of a written transcript. If the District Judge does not approve the plan, he is directed to remand the same to the Commission and to "transmit to the Commission *a copy of any evidence received*" (11 U. S. C. A., §205(3)). To contend that it is proper for a District Court to review and pass upon evidence received by the Commission (or for the Commission to consider evidence introduced before the District Court) but that it is improper for a District Judge to review and pass upon purely supplementary evidence introduced before a predecessor judge who died before he could review his decision is absurd,—especially in view of Petitioners' assumption that *this Court* may and should consider all kinds of unverified documentary and other data bearing on Debtor's earnings and assets since the record was closed in the District Court! As a matter of fact, although most District Courts in Section 77 proceedings have made it a practice to receive additional evidence on the hearing upon objections to the plan, there is nothing in the statute which requires that such additional evidence be received and it would appear to be entirely a matter of discretion whether the District Court shall receive such additional evidence.[9]

Moreover, whatever may have been Mr. Meyer's technical right to a rehearing *de novo*, such right was clearly waived by him. Although Mr. Meyer and his associate, Mr.

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[8] *Palmer* v. *Massachuetts*, 308 U. S. 79, 87 (1940).

[9] The courts have recognized that rules of procedure applicable to ordinary jury or non-jury trials upon the death or retirement of the judge do not apply in special statutory proceedings which may be drawn out over many years. See, *In re Nolan's Will*, 63 Atl. 618 (N. J., 1906); *Barton* v. *Burbank*, 138 La. 997, 71 So. 134 (1916); *Matter of Carey*, 24 App. Div. 531 (4th Dept., 1897).

Chubb, made statements at the conference before Judge Moore in April, 1943, which indicated that they believed that they were entitled to a hearing *de novo,* Mr. Meyer clearly indicated that he had no real objection to Judge Moore considering the evidence which had been presented before Judge Davis and that what he really wanted was an opportunity to present *additional evidence;* and the chief question discussed was whether Mr. Meyer had a legal right to present additional evidence.

Thus, Mr. Meyer stated (R. 5155):

> "• • • all I want is an opportunity to introduce this new testimony, an opportunity, if I may use the word, to educate Your Honor as to the facts of this extraordinary case. And I am not here for any other purpose."

Finally, at the very end of the hearing, Mr. Chubb stated specifically (R. 5180):

> "• • • Mr. Meyer has said and I have said that *it is our present intention to take no exception to the use of such testimony as has already been taken.* • • •"

Moreover, neither in his elaborate brief of 242 pages before the District Court dated July 2, 1943, nor in his reply brief of 109 pages dated August 4, 1943, did Mr. Meyer make any contention that the District Court was precluded from considering the evidence which had been introduced before Judge Davis or that by reason of Judge Davis' death he was entitled to a hearing *de novo.* As a matter of fact, many of the contentions in Mr. Meyer's briefs were in whole or in part predicated upon the testimony presented before Judge Davis.

Having thus led the parties and the District Court to believe that he had no objection to Judge Moore considering

the evidence which had been introduced before Judge Davis, obviously Mr. Meyer cannot now be heard to complain that Judge Moore did consider that evidence; and having thereafter failed, at the hearing before Judge Moore on May 31, 1943, to request permission to present additional evidence, pursuant to Judge Moore's order of April 23, 1943 (R. 5182), he cannot now be heard to complain on that score.

3. The Circuit Court of Appeals correctly denied Mr. Meyer's motion to remand.

While the appeals were pending in the court below, the Petitioner Meyer moved to remand the proceedings to the Commission on the ground of newly-discovered evidence, alleged to have been revealed in the complaint in an anti-trust action brought by the United States against the Association of American Railroads and others in August, 1944, in the District Court for the District of Nebraska, and in the so-called "Western Agreement" annexed to said complaint. The court below denied the motion on the ground that Mr. Meyer had been familiar with the Western Agreement for many years and hence that it did not constitute newly-discovered evidence (R. 5571-5573).

Mr. Meyer's attempt to bring this issue before this Court must fail, first, because the denial of a motion for a new trial on the ground of newly-discovered evidence is not reviewable except for manifest abuse of discretion.

> *Royal Ins. Co.* v. *Eastham*, 71 F. (2d) 385 (C. C. A. 5th, 1934), c. d. 293 U. S. 557 (1935);
> *McIntyre* v. *Texas Co.*, 48 F. (2d) 211, 212 (C. C. A. 2d, 1931).

Moreover, the action of the Circuit Court of Appeals was plainly correct. A new trial will not be granted on the ground of newly-discovered evidence unless the moving

party clearly establishes (1) that he did not discover, and by the exercise of reasonable diligence could not discover, the evidence until after the original hearing, and (2) that the evidence is not merely cumulative, but possesses such weight as to indicate that a rehearing would probably produce a different result. *Crow* v. *Dumke*, 142 F. (2d) 635 (C. C. A. 10th, 1944). Mr. Meyer's petition utterly fails to show how the alleged newly-discovered evidence might have affected the Commission's findings. Moreover, the record shows that at least as early as December 22, 1932, Mr. Meyer was familiar with the so-called Western Agreement (Exhibit 225, before the Commission). As a matter of fact, the Western Agreement was more or less public knowledge long before the Debtor's bankruptcy (see testimony of Joseph B. Eastman, Hearings before the Senate Committee on Interstate Commerce on S. 942, 78th Cong., 1st Sess., pp. 831-832, 834).

Conclusion.

The petitions raise no questions of general importance. There is no conflict of decisions and the decision is clearly correct. The petitions should be denied.

Respectfully submitted,

February 22, 1947.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1946

No. 879

SOUTHERN PACIFIC COMPANY, a railroad corporation, Intervener, *Petitioner,*

vs.

BERRYMAN HENWOOD, as Trustee of St. Louis Southwestern Railway Company Lines, et al., *Respondents.*

No. 909

WALTER E. MEYER, Intervener, *Petitioner,*

v.

BERRYMAN HENWOOD, as Trustee of St. Louis Southwestern Railway Company Lines, et al., *Respondents.*

No. 936

ST. LOUIS SOUTHWESTERN RAILWAY COMPANY, a Corporation, Debtor, *Petitioner,*

vs.

BERRYMAN HENWOOD, as Trustee of St. Louis Southwestern Railway Company Lines, et al., *Respondents.*

BRIEF IN OPPOSITION TO PETITIONS FOR WRITS OF CERTIORARI

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BRIEF IN OPPOSITION TO PETITIONS FOR WRITS OF CERTIORARI TO THE CIRCUIT COURT OF APPEALS FOR THE EIGHTH CIRCUIT

The respondent Chemical Bank & Trust Company (hereinafter referred to as the "General and Refunding Trus-

tee"), the successor and sole Trustee under the Debtor's General and Refunding Mortgage dated July 1, 1930, files this brief in opposition to the petitions of the Debtor, Southern Pacific Company and Mr. Walter E. Meyer which request this Court to review the decision of the Circuit Court of Appeals affirming the District Court's order approving the Plan of Reorganization of the Debtor (hereinafter referred to as the "Commission's Plan").

Reports and Opinions Below

The Report and Order of the Interstate Commerce Commission (herein referred to as the "Commission") of June 30, 1941 (R. 3495-3735) are reported in 249 I. C. C. 5, and its Supplemental Report and Order of March 9, 1942 (R. 3736-3820) are reported in 252 I. C. C. 325.

The opinion of the District Court (R. 5183-5212) is reported in 53 F. Supp. 914. The opinion of the Circuit Court of Appeals (R. 5559-5683) is reported in 157 F. (2d) 337.

Jurisdiction

The judgment of the Circuit Court of Appeals was entered August 26, 1946 (R. 5681-5683). Petitions for rehearing were denied October 22, 1946 (R. 5831). The petitions for writs of certiorari were filed, respectively, January 13, 1947 (No. 879), January 18, 1947 (No. 909), and January 21, 1947 (936). The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925 (28 U. S. C. Sec. 347 (a)), and Section 24 of the Bankruptcy Act (11 U. S. C. Sec. 47 (c)).

Statute Involved

The statute involved is Section 77 of the Bankruptcy Act as amended (11 U. S. C. Sec. 205).

STATEMENT

The Scope of This Brief

The General and Refunding Trustee is the sole representative in the reorganization proceedings of the Debtor, of the members of the public who own outright $9,327,500 in principal amount of General and Refunding Bonds.

The General and Refunding Trustee believes that the allocation of securities of the reorganized company to the General and Refunding Bondholders by the Commission's Plan constitutes the minimum treatment to which the General and Refunding Bondholders are entitled. Under the Commission's Plan the brunt of the Debtor's reorganization falls to a great extent on the General and Refunding Bondholders. Any recognition of stockholders of the Debtor by the distribution to them of securities of the reorganized company would most seriously affect the General and Refunding Bondholders and might indeed be made at their expense. It is on this account that the General and Refunding Trustee submits this brief.

The General and Refunding Trustee has studied the briefs in opposition filed herein on behalf of Guaranty Trust Company, Trustee under the Debtor's First Terminal and Unifying Mortgage and by the Protective Committee for holders of the Debtor's First Terminal and Unifying Bonds. In order to avoid repetitious argument, this brief will merely present certain facts relating to the status of the General and Refunding Bondholders in the Debtor's reorganization and a brief argument which points out that full compensatory treatment of the General and Refunding Bondholders will require more than the mere issuance of additional shares of common stock of the reorganized company, sufficient to fill the gap between the amount of the claim on each General and Refunding Bond and the aggregate principal amount and par value of new securities allocated to each such claim by the Commission's Plan.

Status of the General and Refunding Bondholders in the Debtor's Reorganization

Outstanding General and Refunding Bonds

There are outstanding under the General and Refunding Mortgage $39,557,500 principal amount of General and Refunding Bonds, of which

$ 9,327,500	in principal amount are held outright by the public;
23,903,000	in principal amount are pledged to secure the Debtor's notes in the principal amount of $17,882,250 acquired by Southern Pacific Company from Reconstruction Finance Corporation;
4,921,500	in principal amount are pledged to secure notes of the Debtor in the principal amount of $3,500,000 to The Chase National Bank of the City of New York; and
1,405,500	in principal amount are pledged to secure notes of the Debtor in the principal amount of $1,000,000 to the Mississippi Valley Trust Company.
$39,557,500	total principal amount outstanding.

(R. 3780-3781)

Representation of the General and Refunding Bondholders in the Debtor's Reorganization Proceedings

The Chase National Bank of the City of New York and Mississippi Valley Trust Company (herein referred to as "the Banks") are jointly represented in these proceedings by their own counsel, and have actively participated throughout these proceedings in their own interest.

Southern Pacific Company, the holder of most of the Debtor's stock and the pledgee of General and Refunding Bonds, is represented by its own counsel and has filed one of the petitions now being considered.

There have been a number of instances in these proceedings where the interests of the outright owners of General and Refunding Bonds and of the pledgees of such Bonds have not been identical. In each such instance the General and Refunding Trustee has considered the matter solely from the viewpoint of the interests of such outright owners and has urged the Commission and the Courts to adopt the solution which it believed would be most beneficial to them.

Counsel for the Banks and counsel for Southern Pacific Company have made no objection to this practice of the General and Refunding Trustee.

At this stage of the proceedings there is no conflict of interest between the outright owners of General and Refunding Bonds and the pledgees as such. It is true that the Commission's Plan treats the pledgees as if they were outright owners of the pledged General and Refunding Bonds which in principal amount greatly exceed the principal amount of the Debtor's notes for the payment of which General and Refunding Bonds were pledged. It is conceivable that a conflict of interest would arise between the outright owners and pledgees of General and Refunding Bonds if the value of the securities so allocated to the pledgees of the General and Refunding Bonds were to exceed the amounts owed by the Debtor on the notes.

A serious conflict of interest does exist between the outright owners of the General and Refunding Bonds and Southern Pacific Company, as the owner of approximately 87% of the outstanding stock of the Debtor.

Allocation to the General and Refunding Bondholders Proposed in the Commission's Plan

The Commission's Plan proposes that, subject to adjustment for interest payments made on the Debtor's securities after December 31, 1941 (R. 3812), the reorganized company shall issue to the holders of General and Refunding Bonds, both publicly held and pledged, for the claim as of January 1, 1942, of $1,320.59 for principal and interest on each $1,000 in principal amount of such Bonds, the following securities:

$182.23	in principal amount of new Consolidated Mortgage Bonds;
301.78	in par value of new Preferred Stock; and
433.07	in par value of new Common Stock.
$917.08	(R. 3781).

The Commission concluded that the capitalizable assets of the Debtor would not permit the issuance of any securities with respect to $403.51 of the claim of $1,320.59 for principal and interest on each $1,000 General and Refunding Bond (R. 3781). This deficiency has now been reduced to a deficiency of $307.92 on each such Bond by interest payments made since the effective date of the Commission's Plan.

ARGUMENT

The petitioners have failed to meet the burden of showing that full compensatory treatment could be awarded to the General and Refunding Bondholders in a revised Plan.

No representative of the Debtor's stockholders claims that any securities of the reorganized company should be distributed to stockholders of the Debtor in the event that its capitalization remains fixed at $75,000,000. Accordingly, unless Mr. Meyer's contention is adopted and the claim of Southern Pacific Company, as a creditor, is disallowed, any distribution of shares of stock of the reorganized company to the stockholders of the Debtor must be made out of additional shares of common stock to be provided for by increasing the capitalization of the reorganized company above that fixed in the Commission's Plan. Any such increase in the capitalization of the reorganized company would have to be made out of its equity now allocated to the General and Refunding Bondholders and to unsecured creditors.

In distributing securities in its Plan, the Commission first took care of the most senior rights of each class of creditors. Bonds secured by all mortgages of the Debtor senior to the General and Refunding Mortgage (including the First Terminal Bonds pledged under the General and Refunding Mortgage) were given recognition. On the same basis, the General and Refunding Bondholders were awarded Consolidated Mortgage Bonds and preferred stock of the reorganized company in recognition of the first liens of the General and Refunding Mortgage (R. 3778). The entire amount of new Consolidated Mortgage Bonds and all of the shares of new preferred stock were required to satisfy liens senior to the fourth blanket lien of the General and Refunding Mortgage. All that was left for distribution at this point in the allocation was common

stock. All of the common stock was allocated to the General and Refunding Bondholders, both public holders and pledgees, except certain shares which were awarded to the Central Arkansas and Stephenville Bondholders in recognition of their claim as unsecured creditors to a portion of the free assets of the Debtor.

The common stock of the reorganized company therefore represents the residue of the Debtor's assets left after all claims senior to those of the General and Refunding Bondholders are satisfied. If the holders of the Debtor's outstanding stock are to share at all in the securities of the reorganized company, their share will have to come out of this residue.

The foregoing supplemental statement of facts demonstrates that the outright owners of General and Refunding Bonds are required by the Commission's Plan to make many sacrifices. Among other things, they will lose their position as creditors of the Debtor and will become stockholders of the reorganized company except as to the relatively small amount of bonds of the reorganized company to be issued to them.

In spite of the drastic treatment accorded the General and Refunding Bondholders by the Commission's Plan, the General and Refunding Trustee has not attacked it because the Trustee considers that the Commission has recognized all of the liens and other rights of the General and Refunding Bondholders.

The General and Refunding Trustee, however, has attacked the suggestion made in the Court below by the Debtor and Southern Pacific Company that the changed financial condition of the Debtor and the alleged increase in its prospective earning power could be recognized in a revised Plan by filling out the claims of the General and Refunding Bondholders with additional shares of common stock of the reorganized company at the rate of $1.00 in par value of such common stock for each $1.00 of unsatisfied claim and by then issuing the remaining additional shares of new common stock to stockholders of the Debtor.

Full compensatory treatment of the General and Refunding Bondholders might indeed be qualitative instead of quantitative, but the necessity for such treatment is an additional element to be considered in determining whether the improvement in the financial condition of the Debtor and the alleged increase in its earning power require the upsetting of the Commission's Plan which has been declared fair by the Commission and by the Courts below.

CONCLUSION

For the foregoing reason and for the reasons set forth in the carefully considered Reports of the Commission and in the opinions of the Courts below, the General and Refunding Trustee believes that the petitions for writs of certiorari should be denied.

Dated: February 21, 1947.

Respectfully submitted,

ALFRED H. PHILLIPS,
Of Counsel for Chemical Bank & Trust Company, as Successor Trustee under the General and Refunding Mortgage of St. Louis Southwestern Railway Company.